



## **CITY OF DETROIT**

### **A CHALLENGE FACING THE CITY OF DETROIT : FUNDING THE CITY'S RETIREE HEALTH CARE AND PENSION BENEFITS**

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# A CHALLENGE FACING THE CITY OF DETROIT : FUNDING THE CITY'S RETIREE HEALTH CARE AND PENSION BENEFITS

## OVERVIEW – A NATIONAL PERSPECTIVE

The underfunding of pension plans and retiree health care benefits will wreak financial havoc on many states and municipalities long before the more widely discussed bankruptcy of Social Security and Medicare.

## BACKGROUND

Since World War II, there has been a concerted effort to improve the pay and benefits of municipal employees to levels competitive with private industry. While pay has improved and, in many cases, achieves parity with the private sector, pension and health care benefits for many municipal workers are vastly superior to those available in the private sector. In many cases, benefits, including pension benefits and retiree health care benefits, were improved to reach contract settlements – because municipal budgets could not support additional wage increases. Although this strategy postponed cash payouts, there still was a need for funding pension plans to “accumulate” sufficient funds to pay for pensions. Although not required by law, fiscal prudence would suggest similar funding for retiree health care benefits.

## TRENDS – 1960 TO 2000

At the same time, the number of state and local employees and retirees has increased significantly. Consider the table below :

	YEAR					INCREASE FROM 1960 TO 2000
	1960	1970	1980	1990	2000	
	(000)	(000)	(000)	(000)	(000)	%
STATE & LOCAL EMPLOYEES	6,387	10,147	13,315	15,263	17,507	174 %
STATE & LOCAL RETIREES	660	1,290	2,607	4,026	5,506	734 %
TOTAL STATE AND LOCAL	7,047	11,437	15,922	19,289	23,013	227 %
TOTAL U.S. POPULATION	180,671	205,052	227,726	249,913	272,945	51 %
STATE & LOCAL EMPLOYEES AND RETIREES AS A % OF U.S. POPULATION	3.9%	5.6%	7.0%	7.7%	8.4%	--
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MEMO:						
CIVILIAN (NON-TAX SUPPORTED) EMPLOYMENT	55,923	64,456	82,130	99,391	113,776	106 %
FEDERAL EMPLOYEES + RETIREES (EXCL. MILITARY)	2,936	3,839	4,573	5,248	5,157	76 %
- % of U.S. POPULATION	1.6%	1.9%	2.0%	2.1%	1.9%	--
SOCIAL SECURITY BENEFICIARIES	14,844	26,229	35,585	39,832	44,596	200 %

Source: Statistical Abstracts of the United States

From 1960 to 2000, the following took place:

- The population of the United States increased by 51%.
- Employment by state and local municipalities increased by 174% -- 3.4 times the rate of population increase.
- The number of state and local retirees increased by 734% -- 14.4 times the rate of population increase.
- The total number of employees plus retirees supported by state and local taxes increased by 227% -- 4.5 times the rate of population increase. Today, one out of every twelve citizens (8.4% of the population) is an employee or retiree of state and local government.

### RECENT DEVELOPMENTS

Beyond 2000, the following has occurred or will occur:

- U.S. Department of Labor statistics show that, in the 18 months from January 2001 through June 2002, a period of economic decline, the number of private, non-farm jobs in the U.S. decreased by over two million. At the same time, public-sector employment continued to rise by an additional 400,000.
- Over the next ten years, the rate of retirements for state and local employees will increase significantly – as the approximately 4.5 million workers hired between 1970 and 1980 retire.

### CONCLUSION

Since 1960, the number of state and local government employees and retirees has escalated far more rapidly than the number of employees and retirees in the Federal Government and in the private sector. On average, state and local governments will have great difficulty expanding their future budgets much beyond the rate of inflation because of the great difficulty of raising tax rates or instituting new taxes. However, the costs for pensions and retiree health care will continue to escalate rapidly over the next ten years. These trends will add significantly to the serious financial challenges already facing many, if not most, municipalities.

In May 2004, Perry Young, a director at Standard and Poor's, stated to the National Federation of Municipal Analysts that "The pension liability time bomb has stopped ticking.....it has already exploded." What is increasingly obvious is that the pension liability time bomb is being accompanied by a "retiree health care" time bomb.

There is a pension and retiree health care crisis in America today that threatens the financial viability of many corporations, most major cities, many states, and even the Federal Government. To quote David Osborn and Ted Gaebler in their book titled *Reinventing Government*, “Our governments are in deep trouble today” – and this book was written in 1993 !

### COST TRENDS

Most state and local government employees are eligible for “defined benefit” pensions, and for retiree health care benefits, while fewer private sector employees are eligible for similar benefits. As a result, the crisis is greater for state and local governments than for the private sector. Consider the following:

- According to the Bureau of Labor Statistics, in 2003, state and local government employees averaged \$23.56 per hour compared with \$16.49 per hour for private sector employees. This higher average cost also translates into higher average pension payouts.
- 90% of municipal employees (which make up about 13% of the workforce) receive defined benefit pensions. This is unchanged over the last decade. Only 17% of private sector employees receive defined benefit pensions, down from 40% in 1980.<sup>1</sup>
- 82% of state and local municipal governments (for larger cities) offer retiree health care benefits (to pre Medicare-eligible retirees)<sup>2</sup>. This compares with less than 12% for the private sector.<sup>3</sup>
- According to the American Federation of State, County and Municipal Employees, the average public-sector employee now collects an annual pension benefit of 60% of final pay after 30 years on the job. (If he is one of the 20% of public-sector employees who are not eligible to collect Social Security, he receives 75% of final pay after 30 years.) Of the private sector employers that still offer traditional defined benefit pensions, the average benefit is equal to only 45% of final pay after 30 years.<sup>1</sup>
- About 80% of government retirees receive pensions that increase each year to keep pace with the cost of living—but such inflation protection is almost non-existent in corporate plans.<sup>1</sup>

Dallas Salisbury, the President of the Employee Benefit Research Institute recently stated, “The public employee, no matter who you compare him to, has become the dominant sector of the labor force that is well-pensioned and well-benefited. At what point, vis-à-vis tax burden, does the non-pensioned public start to pay attention to that as votes ?”

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Footnotes: see page 33

## INTRODUCTION

The Auditor General's Office of the City of Detroit has engaged J.L. Boyle International (i) to assess the adequacy and the impact of funding for the City's pension and retiree health care benefits, (ii) provide benchmarks to compare the City's funding and assumptions with other municipalities, and (iii) to recommend cost reduction strategies. Although this report does, of necessity, include statistics and employment costs unrelated to retirement, the emphasis is on retirement costs for both current employees and current retirees.

The crisis that the City of Detroit is facing is also being faced by many other municipalities both large and small. Primarily, the problem for Detroit -- as with most other municipalities -- is due to rapidly increasing costs combined with slower growth in revenue, as shown in the table below:

City of Detroit - General Fund				
			Revenue	Memo: Net
			Over/ (Under)	Add'l Borrowings
Fiscal	Revenue*	Expenditures*	Expenditures	for General Fund
Year	(000)	(000)	(000)	(000)
1998	\$ 1,446,775	\$ 1,406,350	\$ 40,425	\$ 56,857
1999	1,413,753	1,438,235	(24,482)	253
2000	1,501,529	1,511,078	(9,549)	23,675
2001	1,459,340	1,488,739	(29,399)	---
2002	\$ 1,587,828	\$ 1,625,470	(37,642)	1,898
2003**	1,548,609	1,601,368	(52,759)	56,001
2004**	1,679,383	1,757,349	(77,966)	193,547
2005 (Budget)***	1,604,759	1,604,759	---	---
2006 (Budget)***	1,415,307	1,415,307	---	---

Source : City of Detroit Comprehensive Annual Financial Reports

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\* Revenue includes "Other Financing Sources" (including debt issued); expenditures include "Other Financing Uses" (including debt repaid)

\*\* Includes "Special Item- Casino Development Revenues" amounting to \$63,750,000 in 2003 and 38,250,000 in 2004.

\*\*\* The assumption is that budgeted expenditures will equal budgeted revenue

Between the 1998 and the 2006 fiscal years, revenue for the City's General Fund is forecasted to decrease by 2.2%. However, because of declining population, the expenditure per citizen will increase by 6.7% -- from \$1,490 per citizen to \$1,590 per citizen. During that same period, the cost-of-living in the Detroit area will have increased by approximately 22%.

Two of the ongoing major cost increases that are having an increasingly significant adverse effect on the City's budgets are retiree health care benefits and pension benefits. The City has not yet addressed the cost needed to "fund" retiree health care benefits. Assuming retiree health care is a contractually funded benefit (as pensions are), then it is reasonable to fund this benefit

over the working life of the employee – as is done for pension benefits. In fact, the Government Accounting Standards Board (GASB), in GASB Statements No. 43 and No. 45, will require Detroit (and all major cities) to start reporting and expensing the liability for “Other Postemployment Benefits” (of which retiree health care is the main component) for the 2007 Fiscal Year ending June 30, 2007.

## **A PRIMER ON RETIREMENT BENEFIT FUNDING**<sup>4</sup>

Compensation for most public employees in the United States (federal, state, and local) includes benefits designed to enhance their incomes following retirement. These benefits fall into two categories: (1) postemployment income, or pensions, and (2) other postemployment benefits, primarily retiree health care.

**Types of Pension Plans.** Pension benefits are either (1) defined by a formula usually based on employee compensation and length of service (“defined benefit”), or (2) determined by contributions to an employee account that are invested to provide a pool of assets available to the employee following retirement (“defined contribution”). In defined benefit plans, the benefit formula is controlling, and the responsibility for assuring payment of the benefit falls on the employer. In defined contribution plans, the benefit is determined by the amounts contributed and the accumulated earnings on those contributions, with the risk borne by the employee.

**Financing Pension Benefits.** In defined benefit plans, the fiduciary responsibility of the employer is to assure that assets are available to pay the benefits as they come due. One way of doing this is through *cash disbursement funding* (“pay-as-you-go”), in which the benefit is paid to retirees out of current revenues of the governmental unit. While this results in lower initial payments, these payments rise and eventually may make payment of the obligation unaffordable without increased taxes or reductions in other expenditure items. Moreover, pay-as-you-go financing shifts the burden of paying for the benefit forward to future generations, thereby artificially reducing the cost of providing services to those citizens who receive them currently.

To avoid the problems associated with *cash disbursement funding*, most defined benefit plans use *advance funding*, in which the employer makes contributions to a fund based on future pension liability created as employees work and are paid. Actuarial determinations of the cost of benefits arising from current service (“normal cost”) are based on assumptions about factors that affect liability, such as life expectancy, rates of salary change, rates of departure from the work force before retirement, and patterns of timing for retirement. The contribution rate, which is based on these factors plus the investment return on pension fund assets, is computed as a level percent of payroll, which will continue unchanged as long as the actuarial assumptions are borne out by actual experience. This makes the annual contribution predictable and facilitates accurate financial planning. (Note: Pension plans in the private sector, which are governed by ERISA [The Employee Retirement Income Security Act], must use this *advance funding* method).

To the extent that actual experience varies from the actuarial assumptions, there may be gains or losses to the pension fund. Frequently, those variances are attributable to ups and downs in the largely unpredictable markets in which pension funds are invested. In addition, the contribution rate may be affected by such things as early retirement programs or changes in the pension benefit formula. To the extent that the contributions to cover normal costs turn out to be inadequate to cover the projected benefits, the actuarial accrued liability will exceed the assets in the fund, creating an *unfunded actuarial accrued liability*. In order to assure that the funds are available to pay benefits when they arise, actuarially determined contributions in addition to



those necessary to cover normal costs must be made over a period of years, typically 30 or 40, to amortize the unfunded accrued liability.

The existence of an unfunded actuarial accrued liability is not, in and of itself, an indication of funding problems. The relationship between fund assets and accrued liabilities, the ***funding ratio***, will vary over time and is generally not considered an indication of problems unless it is in long-term decline or is very low. A pension plan with a funding ratio of 70 percent, which is increasing, may be healthier than a fund with a funding ratio of 80 percent, but is declining.

**Financing Other Postemployment Benefits (OPEB).** While advance funding is the norm for pension benefits, it is not the norm for other postemployment benefits, which are typically paid for on a cash disbursement basis. When first adopted by governmental units, retiree health care benefits amounted to only a few tenths of a percent of payroll and putting them on a pay-as-you-go basis appeared to be a manageable policy. These benefits now rival pension benefits in their cost, and their funding is becoming a major fiscal problem. The arguments against cash disbursement financing and in favor of advance funding apply equally to pension and OPEB funding. In addition, Government Accounting Standards Board Statement No. 43 (GASB 43) “Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans” requires the valuation of retiree OPEB benefits beginning with, in Detroit’s case, the 2007 Fiscal Year (ending on June 30, 2007).

**What is GASB ?** The Government Accounting Standards Board (GASB) is the agency formed in 1984 to establish a standard of financial accounting and reporting for state and local government entities.

## DEMOGRAPHICS FOR THE CITY OF DETROIT

As stated in many recent news articles, Detroit's population has declined by 51% since 1950 – from 1,850,000 to 899,000, less than Detroit's population in 1920. As the table and chart below show, the number of employees has declined consistent with the population decline – remaining at approximately 1.9 City employees per 100 population.

However, the number of retirees eligible for pensions and retiree health care benefits has steadily increased. The number of retirees per 100 population has increased by 120% from 1975 to 2003 – from 1.0 retiree per 100 population to 2.2 per 100 population, and from 0.5 retirees per employee to 1.1 retirees per employee.

### DEMOGRAPHIC DATA – CITY OF DETROIT

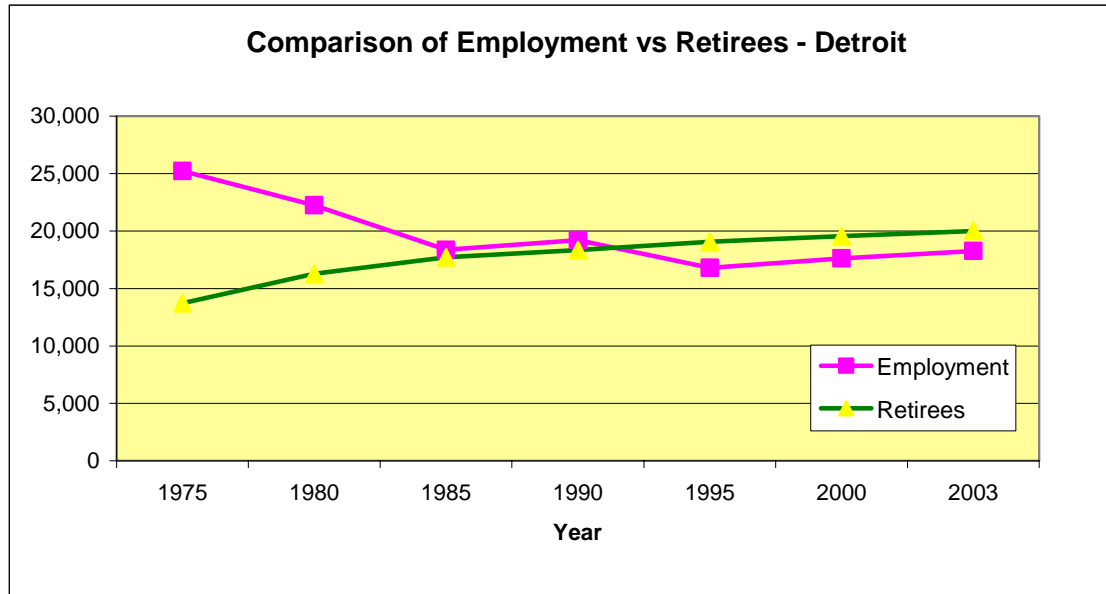
Year	Population*	City Employment**		City Retirees		Retirees Per Employee
		Total Number*	# Per 100 Population	Total Number	# Per 100 Population	
1920	993,000	N/A	N/A	N/A	N/A	N/A
1950	1,850,000	N/A	N/A	N/A	N/A	N/A
1960	1,670,000	N/A	N/A	N/A	N/A	N/A
1970	1,514,000	N/A	N/A	N/A	N/A	N/A
1975	1,355,000 (est.)	25,226	1.9	13,721	1.0	0.5
1980	1,203,000	22,240	1.9	16,284	1.4	0.7
1985	1,115,000 (est.)	18,374	1.6	17,721	1.6	1.0
1990	1,028,000	19,215	1.9	18,344	1.8	1.0
1995	990,000 (est.)	16,799	1.7	19,067	1.9	1.1
2000	951,000	17,628	1.9	19,559	2.1	1.1
2003	911,000	18,267	2.0	19,996	2.2	1.1
2005	899,000 (est.)	17,519	1.9	N/A	N/A	N/A

\* Sources: Statistical Abstract of the U.S., the U.S. Census Bureau, and SEMCOG

\*\* Eligible to participate in the City's pension plans.

While it may be argued that 1.9 City employees per 100 (as of 2005) is high, it has been relatively constant for 30 years.

What has increased both relatively and absolutely is the number of retirees. In 1975, the City had 13,721 retirees – which amounted to (i) 1.0 retiree per 100 population and (ii) 0.5 retirees per employee. In 2003, the City had 19,996 retirees – 1,729 more retirees than employees. This amounted to (i) 2.2 retirees for every 100 population and (ii) 1.1 retirees per employee.



The cost of pensions and retiree health care benefits for this large number of retirees presents the most serious problem for the City of Detroit, and, if not resolved, could force the City into receivership and ultimately bankruptcy.

## **RETIREE HEALTH CARE BENEFITS**

The City of Detroit provides health care benefits (including dental and eye care) to retired employees and their eligible dependents. Significantly, the City does not presently require Medicare-eligible retirees or dependents to use Medicare as their primary health care provider – and coordinate coverage with the City’s health care plan.

The City engages health care providers such as Blue Cross/Blue Shield of Michigan (BCBSM), Health Alliance Plan (HAP), and Omnicare to oversee retiree health-care benefits. The BCBSM rates are based on prior experience with City employees and retirees (essentially a self-insured plan), while the HMO rates are based on community costs (as required by State law).

The contribution rate as a percent of active-member payrolls has been rising steadily, as shown below:

CONTRIBUTION RATES FOR RETIREE HEALTH CARE BENEFITS FOR THE CITY OF DETROIT			
(\$ IN MILLIONS)			
Year	Total Active Payroll*	Retiree Health Care Costs **	
		Cost	% of Payroll
1998	\$ 604.5	\$ 77.4	12.8 %
1999	599.4	87.5	14.6
2000	654.9	99.4	15.2
2001	692.9	103.4	14.9
2002	689.4	119.1	17.3
2003	697.3	132.4	19.0
2004	703.3	145.9	20.7

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\* For participants in the General Retirement System and the Policemen & Firemen Retirement System.

\*\* Includes dental, vision, and life insurance costs.

An analysis of the costs incurred by the City to provide retiree health care benefits for the seven fiscal years ending June 30, 2004 is shown below:

COST TRENDS FOR THE CITY OF  
DETROIT'S RETIREE HEALTH CARE  
(\$ IN MILLIONS)

Fiscal Year	Retiree Health Care Costs <sup>5</sup>	Percentage Increase From Prior Year		Percentage Increase for CPI <sup>6</sup>
		Detroit	Nationwide <sup>2</sup>	
1998	\$77.4	--	6.1%	1.7%
1999	87.5	12.9%	7.3%	2.6%
2000	99.4	13.5%	8.1%	3.6%
2001	\$103.4	4.2%	11.2%	2.7%
2002	119.1	15.0%	14.7%	2.6%
2003	132.4	11.2%	10.1%	2.0%
2004	145.9	10.2%	10.5%	1.6%
6 yr Total	--	88.5%	80.0%	16.0%
6 yr Avg	--	11.1%	10.3%	2.5%

As shown, from 1998 to 2004 Detroit's retiree health care costs increased by 88.5% compared with 80.0% for health care plans nationwide and 16.0% for the Consumer Price Index (CPI).

Over the last seventeen years, costs for health care plans nationwide have increased at an average annual rate of 8.7%. At this rate, retiree health care costs will double every eight years. At the current average rate for the City – 11.1% per year – retiree health care costs would double every 6.5 years.

The table below shows the annualized costs incurred by the City to provide health care benefits (including dental, vision, & life insurance) for its retirees based upon actual costs for the month of September 2004 (Appendix I) and the estimated costs for the 2006 Fiscal Year :

<u>RETIREE HEALTH CARE COSTS</u>		
	<u>September 2004 Annualized</u>	<u>Estimated For the 2006 Fiscal Year</u>
Total Number of Retiree Units*		
Receiving Medical Benefits	16,608 <sup>a</sup>	17,200 (est.)
<u>COST</u>		
Medical	\$ 144,391,600 <sup>a</sup>	\$ 187,755,000 <sup>c</sup>
Dental	6,720,600 <sup>b</sup>	9,090,000 <sup>c</sup>
Vision	2,218,600 <sup>b</sup>	2,173,000 <sup>c</sup>
Life	143,200 <sup>b</sup>	162,000 <sup>c</sup>
TOTAL	<u>\$ 153,474,000</u>	<u>\$ 199,180,000</u>
Average Cost Per Retiree Unit Per Month	\$ 770.00	\$ 965.00

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\* A retiree "unit" includes spouses and other dependents. (Note: Not all retirees participate in the City's retiree-medical programs.)

<sup>a</sup> See Appendix I

<sup>b</sup> Comprehensive Annual Financial Report for 2004 Fiscal Year

<sup>c</sup> City of Detroit Benefits Study by Mercer Human Resource Consulting

The table on the previous page shows that estimated retiree health care benefits for 2004 are \$153.5 million. However, although the recent study by Mercer Human Resource Consulting suggest an annual cost of about \$170.5 million.

With this background, we asked Watkins, Ross & Company, Consulting Actuaries, to estimate the present value of health care benefits provided to employees of the City of Detroit after they retire. Watkins, Ross' calculations were based on the following assumptions:

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Footnotes : See page 12

Mortality 90% of the rates from the 1983 Group Annuity Mortality Table  
(Note: Working populations have lower mortality than general populations)

Discount Rate 5.75% (used to calculate present value of future benefits)

Average Mo. Cost \$965.00 per retiree unit<sup>7</sup> (for 2006 Fiscal Year)

Medical Inflation 12% in first year, declining by one percentage point per year  
to 4% in the ninth year and beyond.

Utilization 90% of those eligible elect coverage from the City

Percent Married 70%

Percent Female 40%

Turnover Rates Same as those used in the 6/30/2003 pension valuations for the City

Retirement Rates	Ages	% Who Retire*	Ages	% Who Retire*
	<36	0.24%	56-60	11.17%
	36-40	0.88%	61-65	14.28%
	41-45	1.22%	66-70	8.61%
	46-50	4.20%	71-74	28.54%
	51-55	6.37%	>74	100.00%

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\*Includes disability retirements.

**Based upon these assumptions, the present value of future postemployment health care benefits (for current employees, former employees, and their eligible dependents) is \$ 7.2 billion.**

This liability consists of:

Active Employees:	
General Employees	\$1,925,608,800
Police & Fire Employees	<u>1,025,621,200</u>
Subtotal	\$2,951,230,000
Retired and Disabled Former Employees:	
General Employees	N/A
Police & Fire Employees	<u>N/A</u>
Subtotal	<u>\$4,218,939,800</u>
Grand Total	<b><u>\$7,170,169,800</u></b>

The total obligation (which is completely unfunded today) consists of two parts:

Accumulated Benefit Obligation (ABO)—The value of benefits allocated to <u>past service</u>	\$6,446,699,700
Future Service Obligation (FSO)--The value of benefits allocated to <u>future service</u>	<u>723,470,100</u>
Total Obligation (Liability)	<b><u>\$7,170,169,800</u></b>

To determine the annual cost to amortize the total obligation for retiree health care benefits, actuarial calculations also determined the following:

Net Periodic Cost (NPC)--	
Cost allocated to current year for <u>active</u> employees*	\$ 121,198,000

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\* Approximately \$7,000 per employee (per year)

Under current accounting rules (GASB Statement No. 43), the total expense charged in the current fiscal year would be:

	Total	Allocable To General Fund**
NPC (with interest at 5.75% to year end)	\$ 128,166,900	\$ 97,791,400
Amortization of ABO over 6 years at 5.75%*	1,300,737,900	992,463,000
Total	<u>\$ 1,428,904,800</u>	<u>\$ 1,090,254,400</u>

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\* Amortization period is the remaining average working life of currently-active employees. This is estimated as FSO divided by NPC which equates to 6 years.

\*\* Based upon retiree units covered by the General Fund – which includes the Department of Transportation and excludes Airport, Building & Safety, Municipal Parking, Water, Sewer, Library, and Housing.

Because the amortization of the ABO shown above would greatly “distort” municipal budgets, GASB 43 allows the ABO to be amortized over longer periods of up to 30 years. On this basis, the expense for the current fiscal year would be:

	Total	Allocable To General Fund
NPC (with interest at 5.75% to year end)	\$ 128,166,900	\$ 97,791,400
Amortization of ABO over 30 years at 5.75%	455,886,400	347,841,300
Total	<u>\$ 584,053,300</u>	<u>\$ 445,632,700</u>

The GASB calculations employ a relatively low rate because GASB 43 and 45 require that the assumed discount rate shall be a rate at which the obligation can be “settled”. Specifically, in the unlikely event that the City ceased to fund its retiree health care obligations in the future, under GASB 43 & 45, there must be a high degree of certainty that the fund assets would be sufficient to pay all of the promised retiree health care benefits. To ensure this, the discount rate used should be equivalent to the interest rate paid on conservative, high quality fixed-income investments, such as AA or AAA bonds.



## **PENSION BENEFIT FUNDING**

Full-time “regular” City employees participate in one of the City’s two pension plans – the Policemen and Firemen Retirement System for police and firefighters and the General Retirement System for all others. (The City also provides a defined contribution plan which is 100% funded by the employees.)

The Michigan Constitution requires that pension benefits be pre-funded and that any unfunded liability arising from adverse actuarial experience or benefit changes such as early retirement programs be amortized. Annual actuarial valuations establish the percentage of payroll necessary to fund the pension benefits. Most of the factors in the actuarial calculations are relatively stable. They include mortality, age patterns of retirement, and projected salary changes for active members.

A factor that is subject to large annual fluctuations is the rate of return on investment on fund assets. That factor is assumed to be 7.9% per year (based on long-term trends in investment markets) for the General Retirement System and 7.8% for the Policemen and Firemen Retirement System. While this assumption has worked fairly well over the long run, large fluctuations in the stock market can, in turn, cause large fluctuations in the contribution percentage, even if the long-term rate assumption is met.

Funding for pension plans is typically expressed as a percent of “active payroll” – essentially base pay for the plan’s active participants. As can be seen in the table on the following page, these percentages generally trended down from 1985 through 2002 but increased significantly in 2003 and 2004

### CONTRIBUTION RATES FOR PENSION BENEFITS FOR CITY OF DETROIT

1995	327.6	209.7	537.3	12.9%	25.9%	18.0%	42.3	54.3	96.6
1996	\$ 360.1	\$ 212.7	#####	11.8%	25.9%	17.0%	\$ 42.5	\$ 55.0	\$ 97.5
1997	382.8	217.6	600.4	14.3%	25.1%	18.2%	54.7	54.5	109.2
1998	387.0	217.5	604.5	13.6%	22.1%	16.7%	52.7	48.1	100.8
1999	383.4	216.0	599.4	14.5%	7.3%	11.9%	55.6	15.7	71.3
2000	\$ 417.2	\$ 237.7	#####	16.0%	8.4%	13.3%	\$ 66.8	\$ 20.0	\$ 86.8
2001	439.6	253.3	692.9	15.5%	5.7%	11.9%	68.1	14.4	82.5
2002	440.7	248.7	689.4	15.4%	3.4%	11.1%	67.8	8.4	76.2
2003	448.6	248.7	697.3	16.3%	26.9%	20.0%	72.9	66.8	139.7
2004	444.6	258.7	703.3	21.6%	26.9%	23.5%	95.9	69.5	165.4

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\* Information obtained from the City's Actuarial Valuations and Comprehensive Annual Financial Reports

\*\*GRS is General Retirement System; P&F is Policemen & Firemen Retirement System

Another major concern for the City of Detroit is the increase in the unfunded actuarial accrued liability as shown below:

### ASSETS AND UNFUNDED ACTUARIAL ACCRUED LIABILITIES FOR THE CITY OF DETROIT'S PENSION PLANS

FISCAL YEAR	ACTUARIAL VALUE OF PENSION PLAN ASSETS			ACTUARIAL ACCRUED LIABILITY			UNFUNDED ACTUARIAL ACCRUED LIABILITY*		
	GRS**	P&F**	TOTAL	GRS**	P&F**	TOTAL	GRS**	P&F**	TOTAL
	(mils.)	(mils.)	(mils.)	(mils.)	(mils.)	(mils.)	(mils.)	(mils.)	(mils.)
1998	\$ 2,582.1	\$ 3,325.9	\$ 5,908.0	\$ 2,814.9	\$ 2,976.8	\$ 5,791.7	\$ 232.8	\$ (349.1)	\$ (116.3)
1999	2,756.6	3,668.3	6,424.9	2,900.4	3,274.1	6,174.5	143.8	(394.2)	(250.4)
2000	2,902.4	3,964.2	6,866.6	3,077.0	3,342.1	6,419.1	174.6	(622.1)	(447.5)
2001	\$ 2,912.1	\$ 3,900.0	\$ 6,812.1	\$ 3,179.6	\$ 3,463.2	\$ 6,642.8	\$ 267.5	\$ (436.8)	\$ (169.3)
2002	2,761.2	3,635.1	6,396.3	3,276.6	3,523.4	6,800.0	515.4	(111.7)	403.7
2003	2,537.7	3,205.5	5,743.2	3,270.7	3,721.6	6,992.3	733.0	516.1	1,249.1
2004	2,470.2 (e)	3,074.5	5,544.7	3,383.9 (e)	3,857.5	7,241.4	913.7 (e)	783.0	1,696.7

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\* Unfunded / (Over-funded)

\*\* GRS is General Retirement System; P&F is Policemen & Firemen Retirement System

As can be seen from the table on the previous page, from 1998 to 2004, the total unfunded actuarial accrued liability deteriorated from an over-funded position of \$116.3 million to an underfunded position of \$1,696.7 million.

On February 4, 2005, the City Council approved the issuance of \$1.2 billion in pension obligation certificates. This will effectively replace a large position of the unfunded liability with general revenue bonds – and will reduce the city’s unfunded pension liability to \$500 million. POCs also represent a “risk arbitrage” – a bet that the costs plus interest on the bonds (plus issuance costs) will be less than the return on investment for the pension fund assets (currently forecasted to be 7.9% for the General Retirement System and 7.8% for the Policemen and Firemen Retirement System).

While studies suggest that over long periods of time equities will outperform bonds by 4% to 5%, that financial arbitrage is not without risks – as the City of Pittsburgh learned when it issued pension obligation certificates in 1996, then failed to address its structural deficit, and then suffered losses from the 38% drop in stock values in 2001 and 2002. However, Pittsburgh’s issuance of POCs had many “negatives” that are not a concern for Detroit. Among them:

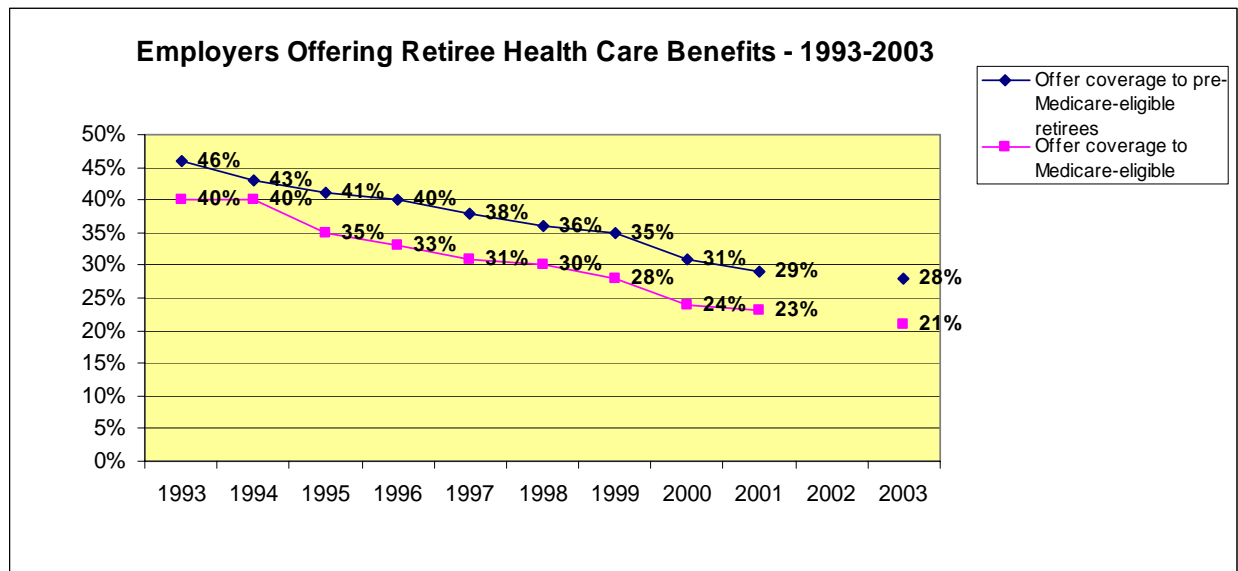
- Pittsburgh’s pensions, prior to issuing the POCs, had a funding ratio of only 19% vs. 77% for Detroit (as of June 30, 2004). This makes the POCs a much smaller percentage of pension assets for Detroit.
- Pittsburgh’s POCs were equal to over 200% of the pre-POC pension assets vs. 22% for Detroit.
- Pittsburgh’s POCs were issued at a time of relatively high interest rates; Detroit’s POCs will be issued at a time of relatively low interest rates.
- Pittsburgh’s POCs were non-callable. Detroit’s POCs are callable.

After the POCs are issued, it would be prudent for the City to determine the health of its pension funds by monitoring its “true” unfunded liability which is the sum of the balance for the pension obligation certificates plus the unfunded liabilities for the pension plans. And, it would be imprudent to use this “relief” to take the pressure off attacking the City’s structural deficit – including the need to significantly reduce employment costs.

## BENCHMARKS

### Retiree Health Care Benefits

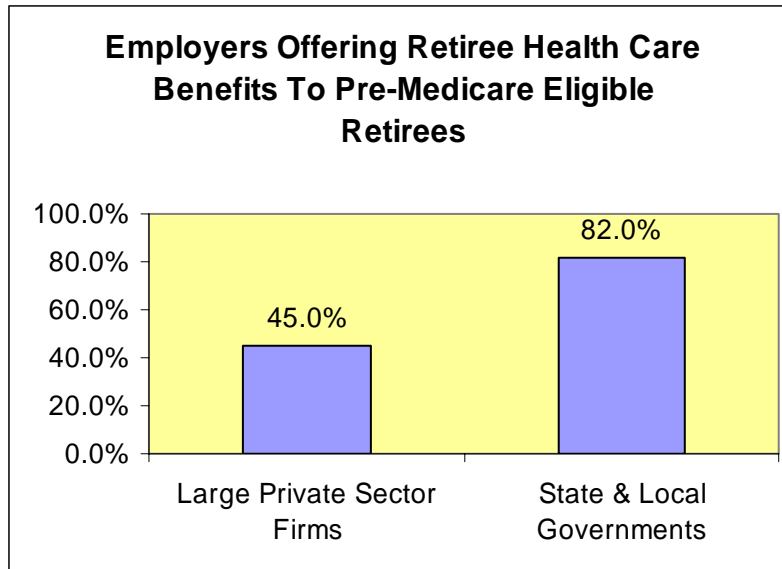
In 2003, Mercer Human Resource Consulting conducted a survey titled “National Survey of Employer-Sponsored Health Plans”. One area of review was the general availability of retiree health care benefits across various regions and company sizes. The percentage of firms offering retiree health care benefits has declined significantly over time. Since 1993 large employers offering health care benefits to pre-Medicare-eligible retirees dropped from 46% to 28%; those offering a plan to Medicare-eligible retirees declined from 40% to 21%. (Note: According to the Employee Benefit Research Institute, less than 12% of all private-sector employees offer retiree health care benefits.)



Source: Mercer National Survey of Employer-Sponsored Health Plans 2003

Note: No data available for 2002

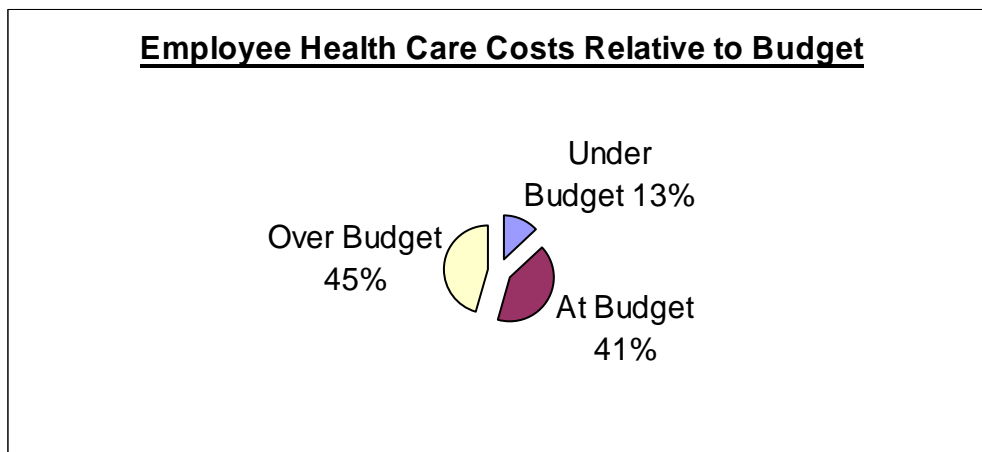
The larger the employer, the more likely it was to provide retiree health care benefits. 45% of employers with 10,000-19,999 employees (the range in which Detroit would fall) offered pre-Medicare-eligible retiree health care benefits. In contrast, 82% of state and local governments offer retiree health care benefits to pre-Medicare-eligible retirees.



Source: Mercer National Survey of Employer-Sponsored Health Plans 2003

Nationally, it is projected that health care costs will continue to increase by double digit rates. The National Health Care Trend Survey from Buck Consultants reported that preferred provider organizations (PPOs) expected 15.2% cost increases, point-of-service (POS) plans expected 15.0% increases, and HMOs expected 14.0% increases for 2004. This is on track with the runaway inflation in health care costs over the last several years.

For health care plans nationwide, the average annual rate of increase in health care costs from 1987 through 2003 was 8.7%.<sup>2</sup> This was almost three times the 3.0% average annual increase in the CPI from 1987 to 2003. Despite much publicity regarding these large increases many employers have been taken by surprise in covering health care expenses. 45% of employers reported that their actual costs exceeded budgeted amounts.



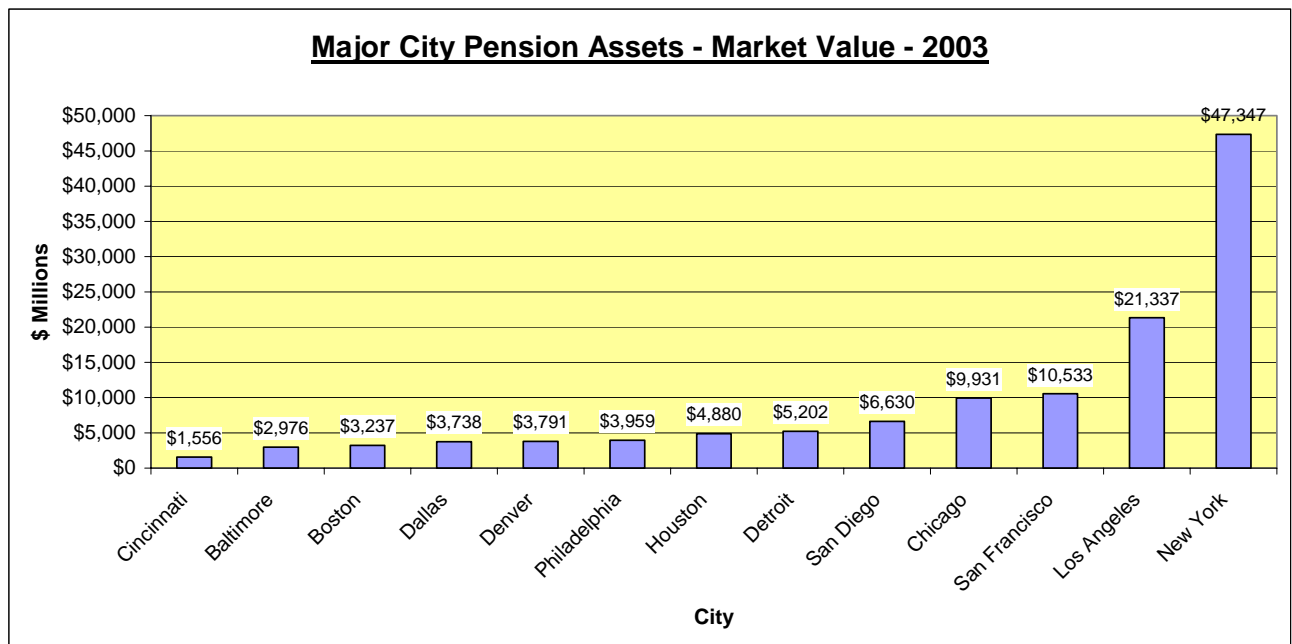
Source: Watson Wyatt Worldwide and the Washington Business Group on Health, March 6, 2003

From 1998 to 2004, the City of Detroit has seen its retiree health care costs increase by 88.5% compared with an increase of 80.0% for health care plans nationwide and 16.0% for the CPI. For the City, this represents an annual rate of increase in retiree health care benefit costs of 11.1% compared with 10.3% for health care plans nationwide.

### **Pension Benefits**

With 90% of municipal employees nationwide eligible for defined-benefit pensions, Detroit is typical in this regard.

In terms of size, Detroit's pension funds are among the largest in the United States – ranking 6<sup>th</sup> among major cities.<sup>8</sup> (See Table below)



City	Pension Assets <sup>8</sup> (Mils)	Population		Pension Assets Per Citizen
		Number (000)	Rank	
San Francisco	\$10,533	752	14	\$14,013
Denver	\$3,791	557	26	\$6,800
New York	\$47,347	8,086	1	\$5,856
<b>Detroit</b>	<b>\$5,202</b>	<b>911</b>	<b>10</b>	<b>\$5,708</b>
Los Angeles	\$21,337	3,820	2	\$5,586
Boston	\$3,237	582	23	\$5,566
San Diego	\$6,630	1,267	7	\$5,234
Cincinnati	\$1,556	317	56	\$4,903
Baltimore	\$2,976	651	18	\$4,570
Chicago	\$9,931	2,869	3	\$3,461
Dallas	\$3,738	1,208	9	\$3,094
Philadelphia	\$3,959	1,479	5	\$2,676
Houston	\$4,880	2,010	4	\$2,428

Based upon this table, Detroit's pension assets per citizen are 4<sup>th</sup> highest among major cities.

Based upon studies done by Wilshire Research<sup>8,9</sup> (Appendices II & III), it would appear that the investment return rate used in Detroit's pension plans are comparable to those used by other municipalities – the GRS rate is 7.9% and the Policemen and Firemen rate is 7.8% compared with an average of 8.0% for City and County Retirement Systems and 7.8% for State Retirement Systems. In addition, the funding method used by the City's Pension Fund (Entry Age Normal) is the most frequently used method by state and local governments.

With regard to the City's unfunded liability (market value of fund assets minus actuarial accrued liability) the City did not fare as well. The table below summarizes rankings for Detroit's two pension funds :

**RANKING OF FUNDING RATIOS FOR  
DETROIT'S PENSION FUNDS FOR 2003**

	<u>GRS*</u>	<u>P&amp;F*</u>
Unfunded Liability (Market Value of Assets Minus Liabilities (\$ million))	\$(947)	\$(843)
Rank out of 104 Systems	86	83
Funding Ratio (Market Value divided by Liabilities)	71%	77%
Rank out of 104 Systems	87	72
<hr/>		
Average funding ratio for 104 City & County Systems <sup>8</sup>	85%	
Average funding ratio for 123 State Systems <sup>9</sup>	79%	
Average funding ratio for S&P 500 Companies <sup>10</sup>	82%	

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 \* GRS is General Retirement Systems; P&F is Policemen and Firemen Retirement System.



## **ESTIMATED FUTURE CONTRIBUTIONS FOR RETIREE BENEFITS**

In order to estimate an “ongoing” contribution rate, it is necessary to make several assumptions. The key assumptions are :

- Health care will continue to be financed on a pay-as-you-go basis until 2008 when GASB 43 and GASB 45 require valuations and accounting on an advance funding basis.
- Although, in principle, the changes in Medicare benefits are likely to generate some savings for the system, no estimates are available at this time. Although savings resulting from the changes will lower the projected contribution rates, the increases in the contribution rate are not likely to be materially affected.
- Health care costs for retirees are projected to increase at 16.8% per year for 2005 and 2006. These cost increases will be driven by increases in the number of retirees and increases in the costs of health care. After FY 2006, it is assumed that the increases will conform to the assumptions in the valuation – 12% in 2007 scaling down to 4% per year after 8 years.
- For employees in the General Retirement System and the Policemen & Firemen Retirement System; assumes 4.3% of active employees are laid off in late FY 2005 & FY 2006 (from 17,519 to 16,765 for the City as a whole), reducing active payroll cost by 2.9%. After 2004, assumes annual pay increases of 4.4%.
- Pay increases of 4.4% per year. (This is the average of rates used in pension-plan valuations. However, because of the City’s continuing fiscal crisis, we believe this rate of pay increase will not be sustainable.)

### **RETIREE HEALTH CARE**

If health care benefits were pre-funded from FY 2008 forward and the unfunded actuarial accrued liability amortized over 30 years, the required contribution rate would be 75.1% of payroll in 2008 – but decline to 44.8% in 2020 and 29.1% in 2030. The chart on the following page compares funding percentages under level payment versus pay-as-you-go calculations. The budgetary savings achieved by postponing contributions into the future will place future benefits at risk, just as with Social Security and Medicare.

**CONTRIBUTION RATES FOR RETIREE HEALTH CARE BENEFITS FOR THE CITY OF DETROIT**  
**PAY-AS-YOU-GO VS. LEVEL CONTRIBUTION RATES**  
(\$ in Millions)

Fiscal Year	Total		Projected Retiree Health Care Costs		Projected Retiree Health Care Costs		Actual/Proj. Health Care Cost Increases***
	Active Payroll*	Pay-as-You-Go Basis		Level Payments**			
		Cost	% of Payroll	Cost	% of Payroll		
1998 A	\$ 604.5	\$ 77.4	12.8%	\$ -	-	-	
1999 A	599.4	87.5	14.6%	-	-	13.0%	
2000 A	654.9	99.4	15.2%	-	-	13.6%	
2001 A	692.9	103.5	14.9%	-	-	4.1%	
2002 A	689.4	119.1	17.3%	-	-	15.1%	
2003 A	697.3	132.4	19.0%	-	-	11.2%	
2004 A	703.3	145.9	20.7%	-	-	10.2%	
2005 P	709.3	170.5	24.0%	-	-	16.9%	
2006	713.8	199.2	27.9%	-	-	16.8%	
2007	745.2	223.1	29.9%	-	-	12.0%	
2008	778.0	247.6	31.8%	584.1	75.1%	11.0%	
2009	812.3	272.4	33.5%	584.1	71.9%	10.0%	
2010	848.0	296.9	35.0%	584.1	68.9%	9.0%	
2011	885.3	320.7	36.2%	584.1	66.0%	8.0%	
2012	924.3	343.1	37.1%	584.1	63.2%	7.0%	
2013	964.9	363.7	37.7%	584.1	60.5%	6.0%	
2014	1,007.4	381.8	37.9%	584.1	58.0%	5.0%	
2015	1,051.7	397.1	37.8%	584.1	55.5%	4.0%	
2016	1,098.0	413.0	37.6%	584.1	53.2%	4.0%	
2017	1,146.3	429.5	37.5%	584.1	51.0%	4.0%	
2018	1,196.7	446.7	37.3%	584.1	48.8%	4.0%	
2019	1,249.4	464.6	37.2%	584.1	46.8%	4.0%	
2020	1,304.4	483.2	37.0%	584.1	44.8%	4.0%	
2021	1,361.8	502.5	36.9%	584.1	42.9%	4.0%	
2022	1,421.7	522.6	36.8%	584.1	41.1%	4.0%	
2023	1,484.2	543.5	36.6%	584.1	39.4%	4.0%	
2024	1,549.5	565.2	36.5%	584.1	37.7%	4.0%	
2025	1,617.7	587.8	36.3%	584.1	36.1%	4.0%	
2030	2,006.4	715.2	35.6%	584.1	29.1%	4.0%	

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\*For employees in the General Retirement System and the Policemen & Firemen Retirement System; assumes 4.3% of active employees are laid off in late FY 2005 & FY 2006 (from 17,519 to 16,765 for the City as a whole), reducing active payroll cost by 2.9%.  
After 2004, assumes annual pay increases of: 4.4%

\*\*Level payments would begin in fiscal year 2008 in accordance with GASB Statement No. 45

\*\*\*Retiree health care cost projections are based upon assumptions used in actuarial valuation of retiree health care costs

## PENSION BENEFITS

If investments are assumed to generate market value returns of 7.9% for the General Retirement System and 7.8% for the Policemen & Firemen Retirement System each year, it will take several years before fund assets reach the same value as prior to the 2001-2002 downturn (adjusted for other factors such as contributions and benefit payments). Even after a positive investment return in 2003, the value of fund assets is less than it was in 1999. The effects of the two bad market years (2001 and 2002) will continue to adversely affect the contribution rate for at least several years into the future.

We are assuming that the City does issue \$1.2 billion in pensions obligation certificates – which was approved by City Council on February 4, 2005 and which is estimated to provide savings of \$277 million over 14 years commencing with the 2006 Fiscal Year.

## PROJECTED FUTURE CONTRIBUTION RATES

Projecting contribution rates into the future carries some risk. Actuarial assumptions are just that: assumptions. Most of the assumptions involve factors that change gradually, such as life expectancy and the average age of employees who retire. Layoffs certainly could affect rates of retirement. Factors such as the performance of investments, issuance of pension obligation certificates, and benefit changes introduce more uncertainty into the calculations.

**Based upon the estimates in the table on the following page, contribution rates for retiree health care and pensions combined will continue their upward trend until they peak in 2008 at 112.1% of payroll on a reporting basis. After 2008, the estimated contribution rates would gradually decline to 46.1% by 2030. On a cash basis, total contributions are estimated to be 68.8% of payroll in 2000 – and peak at 70.6% in 2012. Then the rate would gradually decline to 52.6% in 2030, when the total cash outlay would be \$1,056 million.**

CONTRIBUTION RATES FOR RETIREE HEALTH CARE BENEFITS (GASB 45) AND PENSIONS  
FOR THE CITY OF DETROIT  
(\$ in Millions)

Fiscal Year	Total Active Payroll*	Estimated Retiree Health Care Costs**		Estimated Pension Contributions***		Total Contributions		Memo: Estimated Cost for General Fund Employees****		
		GASB 45	% of Payroll	Cost	% of Payroll	Cost	% of Payroll	Health Care	Pension	Total
1998	\$ 604.5	\$ 77.4	12.8%	\$ 100.8	16.7%	\$ 178.2	29.5%	\$ 59.1	\$ 76.9	\$ 136.0
1999	599.4	87.5	14.6%	71.3	11.9%	158.8	26.5%	66.8	54.4	121.2
2000	654.9	99.4	15.2%	86.8	13.3%	186.2	28.4%	75.8	66.2	142.1
2001	692.9	103.5	14.9%	82.5	11.9%	186.0	26.8%	79.0	62.9	141.9
2002	689.4	119.1	17.3%	76.2	11.1%	195.3	28.3%	90.9	58.1	149.0
2003	697.3	132.4	19.0%	139.7	20.0%	272.1	39.0%	101.0	106.6	207.6
2004	703.3	145.9	20.7%	165.4	23.5%	311.3	44.3%	111.3	126.2	237.5
2005	709.3	170.5	24.0%	197.8	27.9%	368.3	51.9%	130.1	150.9	281.0
2006	713.8	199.2	27.9%	236.6	33.1%	435.8	61.1%	152.0	180.5	332.5
2007	745.2	223.1	29.9%	282.9	38.0%	506.0	67.9%	170.2	215.9	386.1
2008	778.0	584.1	75.1%	287.7	37.0%	871.8	112.1%	445.7	219.5	665.2
2009	812.3	584.1	71.9%	292.8	36.0%	876.9	108.0%	445.7	223.4	669.1
2010	848.0	584.1	68.9%	298.1	35.2%	882.2	104.0%	445.7	227.5	673.1
2011	885.3	584.1	66.0%	303.6	34.3%	887.7	100.3%	445.7	231.6	677.3
2012	924.3	584.1	63.2%	309.4	33.5%	893.5	96.7%	445.7	236.1	681.7
2013	964.9	584.1	60.5%	315.4	32.7%	899.5	93.2%	445.7	240.7	686.3
2014	1,007.4	584.1	58.0%	321.6	31.9%	905.7	89.9%	445.7	245.4	691.0
2015	1,051.7	584.1	55.5%	328.3	31.2%	912.4	86.8%	445.7	250.5	696.2
2016	1,098.0	584.1	53.2%	335.1	30.5%	919.2	83.7%	445.7	255.7	701.3
2017	1,146.3	584.1	51.0%	342.3	29.9%	926.4	80.8%	445.7	261.2	706.8
2018	1,196.7	584.1	48.8%	349.7	29.2%	933.8	78.0%	445.7	266.8	712.5
2019	1,249.4	584.1	46.8%	357.5	28.6%	941.6	75.4%	445.7	272.8	718.4
2020	1,304.4	584.1	44.8%	365.7	28.0%	949.8	72.8%	445.7	279.0	724.7
2021	1,361.8	584.1	42.9%	244.9	18.0%	829.0	60.9%	445.7	186.9	632.5
2022	1,421.7	584.1	41.1%	253.9	17.9%	838.0	58.9%	445.7	193.7	639.4
2023	1,484.2	584.1	39.4%	263.2	17.7%	847.3	57.1%	445.7	200.8	646.5
2024	1,549.5	584.1	37.7%	272.8	17.6%	856.9	55.3%	445.7	208.1	653.8
2025	1,617.7	584.1	36.1%	282.9	17.5%	867.0	53.6%	445.7	215.9	661.5
2030	2,006.4	584.1	29.1%	340.4	17.0%	924.5	46.1%	445.7	259.7	705.4

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\* For employees in the General Retirement System and the Policemen & Firemen Retirement System; assumes 4.3% of active employees are laid off in late FY 2005 & FY 2006 (from 17,519 to 16,765 for the City as a whole), reducing active payroll cost by 2.9%. After 2004, assumes annual pay increases of 4.4%

\*\* Pay-as-you-go basis through FY 2007; level payments beginning in FY 2008. Contributions include payments on Pension Obligation Certificates (\$129.1 million per year) commencing in FY 2007 and ending in FY 2020.

\*\*\* Actual pension contributions through FY 2004; estimated pension contributions thereafter (Includes payments on POCs and amortization of remaining unfunded actuarial accrued liability)

\*\*\*\* Assumed to be 76.3% of total costs for City. The General Fund includes the Department of Transportation and excludes the Airport, Building and Safety, Municipal Parking, Water, Sewer, Library, and Housing.

CONTRIBUTION RATES FOR RETIREE HEALTH CARE BENEFITS (CASH BASIS) AND PENSIONS FOR THE CITY OF DETROIT (\$ in Millions)										
Fiscal Year	Total Active Payroll*	Estimated Retiree Health Care Costs**		Estimated Pension Contributions***		Total Contributions		Memo: Estimated Cost for General Fund Employees****		
		Cash Basis	% of Payroll	Cost	% of Payroll	Cost	% of Payroll	Health Care	Pension	Total
1998	\$ 604.5	\$ 77.4	12.8%	\$ 100.8	16.7%	\$ 178.2	29.5%	\$ 59.1	\$ 76.9	\$ 136.0
1999	599.4	87.5	14.6%	71.3	11.9%	158.8	26.5%	66.8	54.4	121.2
2000	654.9	99.4	15.2%	86.8	13.3%	186.2	28.4%	75.8	66.2	142.1
2001	692.9	103.5	14.9%	82.5	11.9%	186.0	26.8%	79.0	62.9	141.9
2002	689.4	119.1	17.3%	76.2	11.1%	195.3	28.3%	90.9	58.1	149.0
2003	697.3	132.4	19.0%	139.7	20.0%	272.1	39.0%	101.0	106.6	207.6
2004	703.3	145.9	20.7%	165.4	23.5%	311.3	44.3%	111.3	126.2	237.5
2005	709.3	170.5	24.0%	197.8	27.9%	368.3	51.9%	130.1	150.9	281.0
2006	713.8	199.2	27.9%	236.6	33.1%	435.8	61.1%	152.0	180.5	332.5
2007	745.2	223.1	29.9%	282.9	38.0%	506.0	67.9%	170.2	215.9	386.1
2008	778.0	247.6	31.8%	287.7	37.0%	535.3	68.8%	188.9	219.5	408.4
2009	812.3	272.4	33.5%	292.8	36.0%	565.2	69.6%	207.8	223.4	431.2
2010	848.0	296.9	35.0%	298.1	35.2%	595.0	70.2%	226.5	227.5	454.0
2011	885.3	320.7	36.2%	303.6	34.3%	624.3	70.5%	244.7	231.6	476.3
2012	924.3	343.1	37.1%	309.4	33.5%	652.5	70.6%	261.8	236.1	497.9
2013	964.9	363.7	37.7%	315.4	32.7%	679.1	70.4%	277.5	240.7	518.2
2014	1,007.4	381.8	37.9%	321.6	31.9%	703.4	69.8%	291.3	245.4	536.7
2015	1,051.7	397.1	37.8%	328.3	31.2%	725.4	69.0%	303.0	250.5	553.5
2016	1,098.0	413.0	37.6%	335.1	30.5%	748.1	68.1%	315.1	255.7	570.8
2017	1,146.3	429.5	37.5%	342.3	29.9%	771.8	67.3%	327.7	261.2	588.9
2018	1,196.7	446.7	37.3%	349.7	29.2%	796.4	66.5%	340.8	266.8	607.7
2019	1,249.4	464.6	37.2%	357.5	28.6%	822.1	65.8%	354.5	272.8	627.3
2020	1,304.4	483.2	37.0%	365.7	28.0%	848.9	65.1%	368.7	279.0	647.7
2021	1,361.8	502.5	36.9%	244.9	18.0%	829.0	60.9%	383.4	186.9	570.3
2022	1,421.7	522.6	36.8%	253.9	17.9%	776.5	54.6%	398.7	193.7	592.5
2023	1,484.2	543.5	36.6%	263.2	17.7%	806.7	54.4%	414.7	200.8	615.5
2024	1,549.5	565.2	36.5%	272.8	17.6%	838.0	54.1%	431.2	208.1	639.4
2025	1,617.7	587.8	36.3%	282.9	17.5%	870.7	53.8%	448.5	215.9	664.3
2030	2,006.4	715.2	35.6%	340.4	17.0%	1,055.6	52.6%	545.7	259.7	805.4

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\* For employees in the General Retirement System and the Policemen & Firemen Retirement System; assumes 4.3% of active employees are laid off in late FY 2005 & FY 2006 (from 17,519 to 16,765 for the City as a whole), reducing active payroll cost by 2.9%. After 2004, assumes annual pay increases of 4.4%

\*\* Pay-as-you-go basis through FY 2007; level payments beginning in FY 2008. Contributions include payments on Pension Obligation Certificates (\$129.1 million per year) commencing in FY 2007 and ending in FY 2020.

\*\*\* Actual pension contributions through FY 2004; estimated pension contributions thereafter (Includes payments on POCs and amortization of remaining unfunded actuarial accrued liability)

\*\*\*\* Assumed to be 76.3% of total costs for City. The General Fund includes the Department of Transportation and excludes the Airport, Building and Safety, Municipal Parking, Water, Sewer, Library, and Housing.

## **POLICY OPTIONS AND COST-SAVING RECOMMENDATIONS**

### **LEGAL ENVIRONMENT**

Under present laws, the City is limited in its flexibility to change present retiree health care benefits. The November 2003 report to the City developed by Deloitte Consulting entitled “Pre-1992 General Retirees Study” (based upon a legal opinion from Stevenson Keppelman Associates) states that :

- The City cannot change retiree health care benefits (except for minimal cost containment changes) for retirees covered by collective bargaining agreements at retirement.
- The City may be able to change retiree health care benefits for retirees not covered by collective bargaining agreements at retirement. Because of the City’s longstanding practice of providing the same benefits for union and non-union retirees, we believe that the City risks significant liability if it attempts to change retiree health care benefits for non-union retirees.

With respect to present employees, the City can change their retiree health benefits provided that the changes are negotiated in a future collective bargaining agreement. Note that with respect to municipal police and firefighters (who are legally prohibited from striking), Michigan’s Public Act 312 requires compulsory arbitration for the resolution of disputes.

If necessary to achieve required cost savings, the City could enter into receivership and then, if necessary, declare bankruptcy under Chapter 9 of the Federal Bankruptcy Act. Municipal bankruptcies have long been controversial and are subject to conflicting Federal and State laws and even conflicting laws within the State of Michigan (Appendix IV describes the steps required to file Chapter 9 and its impact on pension and other benefits.)

The ability to change retiree health care and pension benefits for both present retirees and present employees is summarized below:

	PRESENT RETIREES		PRESENT EMPLOYEES	
STATUS	UNIONIZED	NON-UNION	UNIONIZED	NON-UNION
PRESENT SITUATION	Governed by contracts in place at time of retirement	Past practice has been to provide union contractual benefits	Same as present retirees	Same as present retirees
RECEIVERSHIP OR CHAPTER 9 FILING	Ambiguous	Ambiguous	Contracts can be renegotiated or set aside	Contracts can be renegotiated or set aside

Changing pension and/or retiree health care and other postemployment benefits is subject to ambiguities in both federal and state laws either before or after declaration of bankruptcy. Any

action to make changes would undoubtedly be met by lawsuits filed by retiree groups (or pre-emptive lawsuits filed by the City). Because the City could effect these changes immediately and because the resulting lawsuits would not be resolved for an extended time period, the City could realize immediate cost savings. However, if the courts ruled in favor of the retiree groups, the City would have to “pay back” these cost savings at a future date. With regard to pensions, most vested benefits would be guaranteed irrespective of the City’s fortunes because, as of June 30, 2004, the pension fund assets equal 76.5% of the actuarial accrued liabilities.

\* \* \* \* \*

It should be noted that recent trends in court rulings have tended to be more favorable to employers than to retirees. An article entitled “Companies Sue Union Retirees to Cut Promised Health Benefits”, Wall Street Journal, November 11, 2004, states that:

- “The erosion of legal protection for retiree health benefits has been gradual. When medical costs began to rise steeply in the 1980’s, employers first started to cut benefits for salaried retirees.” In the ensuing lawsuits, “courts began accepting company arguments.” After General Motors won a key case involving cuts in benefits for 50,000 retired salaried employees (Robert D. Sprague, et al. v. General Motors Corporation; U.S. Court of Appeals, 6<sup>th</sup> Circuit, January 7, 1998), “salaried retirees have steadily lost in benefits cases ever since. Union retirees were more secure because their benefits were part of negotiated contracts. But after the GM ruling, more employers began to argue that that decision’s logic applied to union retirees, as well, and some courts agreed.”

A more relevant recent development is a February 2004 ruling by the Michigan Court of Appeals in the case of *Alberta Studier v Michigan Public School Employees Retirement Board*.

- In this case, the Court ruled that increases in prescription drug co-payments and deductibles were permissible. The Court specifically stated that it could not rule that health care benefits constitute “accrued financial benefits” under the Michigan Constitution which shall not be diminished or impaired. Thus, retiree health care benefits do not appear to have the same degree of legal protection provided for pension benefits.

#### PENSION COST REDUCTIONS -- RECOMMENDATIONS

Our primary recommendation regarding pension costs is for the City to “migrate” from defined benefit pension plans to defined contribution pension plans. The City’s contribution to these plans would be based upon long term budgets. In addition to reducing costs, defined contribution plans eliminate the uncertainty and the fluctuating contribution requirements caused by varying investment results.

It is worth noting that the State of Michigan replaced its defined benefit plan with a 401(K) defined contribution plan for all employees hired after March 31, 1997.

As mentioned earlier, the City has approved the issuance of \$1.2 billion in pension obligation certificates to “fund” the unfunded actuarial accrued liability for the City’s pension funds. With interest rates still low, this should result in savings over the payback period for the certificates – and the City estimates this savings at \$277 million over fourteen years.

In addition, the City should implement a comprehensive auditing procedure to assure that pension checks are not sent to retirees after they are deceased.

#### RETIREE HEALTH CARE COST REDUCTIONS -- RECOMMENDATIONS

The City of Detroit must quickly identify and implement opportunities to help lower the spiraling health care cost burden – and, in turn, reduce the funding required under GASB 43 & GASB 45.

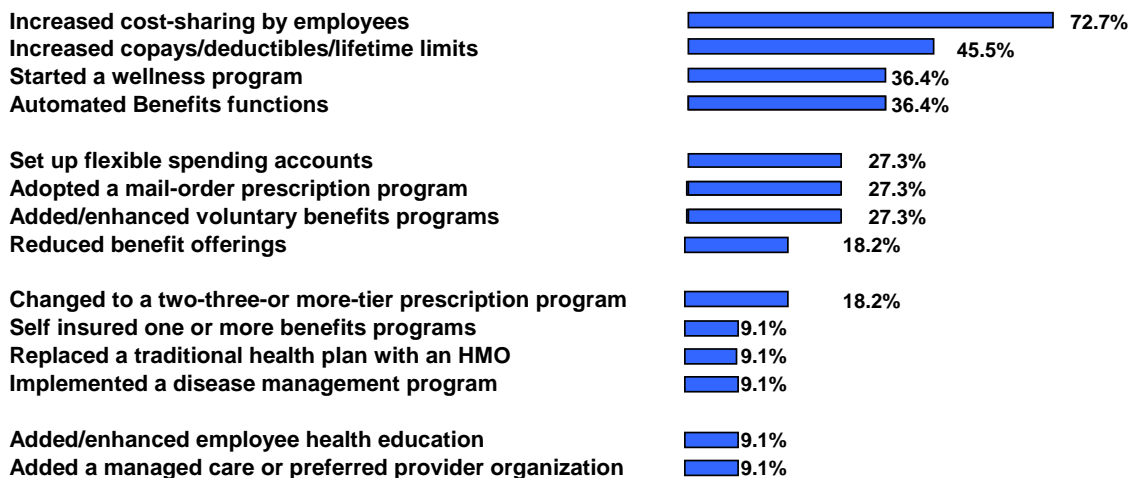
As stated previously (in the Legal Environment Section), making changes to retiree health care benefits is problematic. The City should maintain a broad perspective on cost and should aggressively investigate actions being pursued by the private sector to curb future health care costs.

The first step in developing an effective cost reduction plan is to conduct an organization-specific retiree health care cost analysis. An article in Employee Benefit News, May 2004, entitled “Company-Specific Analysis Identifies Benefit Savings” indicated that at least one-third of all health care costs are caused by overuse, underuse or misuse of health care resources. An organization-specific analysis could include the review of the following data: employee and beneficiary data including plan enrollment, information on health care providers, applicable fee schedules, and medical claims by age, service level, and organization to identify cost trends. Of course, compliance with the rules regarding HIPAA individual privacy is required which will add complexity to cost control efforts.

The Institute of Management & Administration (IOMA) recently conducted a survey to identify areas that organizations are using to control health care benefit costs, shown below:



### **Successful Methods for Controlling Benefits Costs by Government**



Source: Institute of Management & Administration 2004 Benefits Management and Cost Reduction Survey

The number one idea used by almost 73% of surveyed government organizations was increased cost-sharing by employees – and we believe it is critical for the City of Detroit to significantly increase cost-sharing for both employees and retirees.

The results of a recent study by Mercer Human Resource Consulting are telling. For 38% of retiree health care plans, pre-Medicare-eligible retirees paid the full cost of retiree-only coverage. For 49% of plans, the cost was shared between the employer and the retiree. For the remaining 13%, costs were paid by the employer.<sup>2</sup>

In addition to the IOMA cost reduction opportunities the following are additional areas for review;

- Reduce the number of health care plans and choice offerings in order to promote greater price competition among service providers.
- Assure that retirees reaching age 65 enroll in Medicare as their primary claim provider. (This is not now the case with the City's retirees)
- Investigate a new prescription drug program in light of new Federal guidelines.
- Perform, on an ongoing basis, a claims audit program to assure adherence to current policies.
- Enhance employee health education to shift health care costs from the more expensive treatment of diseases to the less expensive prevention. (The City currently has a program to improve clinical outcomes)
- Require working spouses to elect coverage from their employers, if available.

## AN EXPANDED VIEW

Although the purpose of this report is to address funding and other issues related to the City of Detroit's pension and retiree health care benefits, the analyses that we have performed lead us to believe that the City cannot continue to support the existing employee cost structure. To implement a survival program, we believe that the City must take some drastic steps, including consideration of receivership and potentially filing for bankruptcy under Chapter 9.

### Potential Action Steps

According to Maurice P. McTigue, in a lecture entitled "Rolling Back Government: Lessons from New Zealand", Hillsdale College, February 11, 2004, "We're seeing around the world ... a silent revolution, reflected in a change in how people view government accountability." The old view was "that government should spend money in accordance with appropriations. The new (view of) accountability is ... What did we get in public benefits as a result of the expenditure of money? This is a question that has always been asked in business, but has not been the norm for governments."

The actions taken in New Zealand (which has a population of only 4,000,000) also could apply to Detroit. The actions include:

- Holding government agencies and agency managers accountable for results and evaluating them based upon agreed-to performance expectations.
- Identifying what activities each agency should be doing and who should be paying for them (taxpayers, users, consumers, or industry); if the cost of services is not borne by the actual consumers and users, it promotes overuse and devalues the service. (This is the kind of change that results from Activity-Based-Cost analysis)
- Transferring to the private sector all services performed by government that could be more effectively provided by the private sector. In Detroit's case, the following potential transfers should be evaluated:
  - The public lighting department to DTE Energy.
  - The public transportation system
  - Trash collection
  - Snow removal
- Eliminating ineffective subsidies.

As a result of these actions, New Zealand achieved an overall reduction of 66% in the size of government, measured by the number of employees – and the government's share of Gross Domestic Product dropped from 44% to 27%.

If the City acknowledges the depth of its financial crisis and boldly seizes the opportunity to take these and other actions recommended in this report, the City has the opportunity to become a recognized leader in the U.S. for achieving a successful turnaround.

## **CONCLUSION**

The City of Detroit has been a generous employer for many years. However, today, the City faces a major crisis that is reflected in budget shortfalls, a present value for unfunded retiree health care benefits of \$7.2 billion, and high pension costs.

The City cannot rely upon higher taxes or assistance from the State of Michigan to overcome problems of this magnitude. As a result, the City must take drastic action to remain financially viable.

At a minimum, the benchmarks in this report suggest that the City can justify and should implement benefit changes to reflect the less costly benefit levels in private industry.

## **FOOTNOTES/BIBLIOGRAPHY**

1. “The \$360 Billion Outrage”, FORTUNE Magazine, May 31, 2004.
2. “National Survey of Employer-Sponsored Health Plans – 2003 Summary Report” and “May Benefits Report for 2004” by Mercer Human Resource Consulting.
3. “Retiree Health Benefits: Savings Needed to Fund Health Care in Retirement” by Employee Benefit Research Institute, February 2002.
4. “Financing Michigan Retired Teacher Pension and Health Care Benefits”, Citizens Research Council of Michigan, September 2004.
5. City of Detroit – Comprehensive Annual Financial Reports
6. U.S. Bureau of Labor Statistics
7. City of Detroit Benefits Study by Mercer Human Resource Consulting (Dated April 11, 2005)
8. 2004 Wilshire Report on City & County Retirement Systems, October 1, 2004.
9. 2004 Wilshire Report on State Funding Systems, March 12, 2004.
10. 2004 Wilshire Report on Corporate Pension Funding
11. “CITY OF DETROIT – 1992 General Retirees Study”, Deloitte Consulting, November 2003.

## Appendix I

### **Retirees Medical Costs- September 2004**

CARRIER	NUMBER OF PARTICIPANTS	COST
US Health COPS TRUST	2,650	\$2,822,249.79
US Health COPS TRUST	104	123,692.77
BCN - Retired Gen City	565	371,006.05
BCN - Retired Police	30	25,488.23
BCN - Retired Fire	25	22,451.21
BC/BS - Retired Gen City	430	171,590.05
BC/BS - Retired Gen City	5,341	3,361,956.84
BC/BS - Retired Police	827	660,553.76
BC/BS - Retired DSR	105	41,896.71
BC/BS - Retired DSR	409	273,579.72
BC/BS - Retired Fire	1,216	917,752.22
BC/BS - Community Blues - Fire	9	6,724.43
BC/BS - Community Blues - Police	63	41,608.32
Community Blue - General City	204	114,793.58
Community Blue - Police - LSA	222	175,807.45
Community Blue - Fire - LSA	65	53,258.96
CMM Police	1,625	1,156,165.13
CMM Fire	503	361,423.66
HAP - Retired Police	59	50,252.89
HAP - Retired Gen City	1,763	1,078,416.45
HAP - Retired Gen City	13	6,655.52
OmniCare - Retired Fire	7	2,661.66
OmniCare - Retired Police	10	7,411.08
OmniCare - Retired Gen Only	363	185,236.86
Total:	16,608	\$12,032,633.34

Average monthly cost per retiree : \$724.51\*

Annualized Cost : \$144,391,600

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\*Excludes Dental, Vision, and Life Insurance

Source: City of Detroit – Benefits Administration Office

**Appendix IIA**  
**City and County Retirement Systems – Actuarial Summary**<sup>5</sup>  
(\$ Millions)

<b>Retirement System</b>	<b>Actuarial Valuation Date</b>	<b>Funding Method</b>	<b>Interest Rate (%) Assumptions</b>	<b>Market Value of Assets</b>	<b>Actuarial Liabilities</b>	<b>Actuarial Value of Assets</b>
Alameda County ERA	12/31/2003	EAN	8.00	\$3,920	\$3,890	\$3,382
Anne Arundel County ERP	1/1/2004	PUC	8.00	\$377	\$368	\$368
Anne Arundel County PSRP	1/1/2004	PUC	8.00	\$325	\$326	\$311
Anne Arundel County FSRP	1/1/2004	PUC	8.00	\$295	\$302	\$287
Anne Arundel County DODSRP	1/1/2004	PUC	8.00	\$47	\$53	\$46
Arlington County ERS	7/1/2002	EAN	8.00	\$999	\$969	\$1,168
City of Austin ERS	12/31/2003	EAN	7.75	\$1,260	\$1,552	\$1,349
Baltimore County ERS	6/30/2003	EAN	7.88	\$1,623	\$1,831	\$1,741
Baltimore City ERS	6/30/2003	PUC	8.00	\$1,194	\$1,375	\$1,409
Baltimore City Elected Officials RS	6/30/2003	PUC	7.50	\$12	\$14	\$13
City of Baltimore Fire & Police	6/30/2003	PUC	8.25	\$1,770	\$2,287	\$2,205
City of Baton Rouge & Parish ERS	12/31/2003	EAN	8.00	\$814	\$986	\$847
City of Baton Rouge PGT	12/31/2003	AGG	8.00	\$26	\$22	\$26
City of Birmingham R&RS	7/1/2003	EAN	7.50	\$811	\$796	\$786
City of Boston RS	1/1/2004	EAN	8.00	\$3,237	\$5,421	\$3,385
Chicago Municipal EA&BF	12/31/2002	EAN	8.00	\$5,128	\$7,577	\$6,404
Chicago Firemen's ABF	12/31/2003	EAN	8.00	\$1,110	\$2,517	\$1,194
Chicago Policemen's ABF	12/31/2003	EAN	8.00	\$3,693	\$6,581	\$4,040
Chicago Teachers PF	6/30/2003	PUC	8.00	\$9,203	\$11,412	\$10,495
City of Cincinnati RS	12/31/2003	EAN	8.75	\$1,556	\$1,637	\$1,556
Contra Costa County ERA	12/31/2002	EAN	8.00	\$2,366	\$3,678	\$3,297
Dallas ERF	12/31/2002	EAN	8.50	\$1,555	\$2,400	\$1,864
Dallas Police & Fire	1/1/2004	EAN	8.50	\$2,183	\$2,889	\$2,286
Denver ERP	1/1/2002	EAN	8.00	\$1,387	\$1,466	\$1,459
Denver Public Schools RS	1/1/2004	EAN	8.75	\$2,404	\$2,794	\$2,532
Detroit Fire & Police	6/30/2003	EAN	7.80	\$2,878	\$3,722	\$3,206
Detroit General RS	6/30/2003	EAN	7.90	\$2,324	\$3,271	\$2,538
Fairfax County ERS	7/1/2002	EAN	7.50	\$1,717	\$2,052	\$1,854
Fairfax County Police	7/1/2002	EAN	7.50	\$573	\$657	\$628
Fairfax County Uniformed RS	7/1/2002	EAN	7.50	\$618	\$721	\$687
Fort Worth ERF	10/1/2002		8.50	\$1,031	\$1,519	\$1,237
City of Fresno ERS	6/30/2002	PUC	8.25	\$715	\$530	\$749
City of Fresno Fire & Police RS	6/30/2002	EAN	8.25	\$789	\$591	\$815
Fresno County ERA	6/30/2002	EAN	8.00	\$1,566	\$1,932	\$1,675
Fulton County ERS	12/31/2002	EAN	8.20	\$818	\$1,085	\$1,004
Gainesville General EPP	9/30/2003	EAN	9.25	\$213	\$212	\$203
Gainesville Police & Firefighters RP	10/1/2003	EAN	8.50	\$128	\$130	\$126
Grand Rapids GRS	6/30/2003	IEA	7.50	\$269	\$298	\$271
Grand Rapids Police & Fire RS	6/30/2003	IEA	7.00	\$272	\$277	\$270
Houston Firefighters' R&RF	7/1/2002	EAN	8.50	\$1,660	\$1,970	\$1,922
Houston Municipal EPS	7/1/2002	EAN	8.50	\$1,272	\$2,515	\$1,520
Houston Police	7/1/2002	EAN	8.50	\$1,948	\$2,594	\$2,337
Howard County Police & Fire ERP	7/1/2002	PUC	8.00	\$108	\$166	\$124
Howard County RP	7/1/2002	PUC	8.00	\$100	\$114	\$112
Imperial County ERS	6/30/2003	EAN		\$330	\$307	\$301
Jacksonville General EPP	10/1/2003	EAN	8.40	\$1,437	\$1,612	\$1,446
Jacksonville Police & Fire PP	10/1/2003	EAN	8.50	\$704	\$1,146	\$737
Kansas City Police ERS	5/1/2003	EAN	7.75	\$503	\$683	\$611
Kern County ERA	12/31/2002	EAN	8.00	\$1,436	\$1,899	\$1,570
Knox County	1/1/2003	AGG	7.50	\$73	\$85	\$85

## Appendix IIA – Page 2 of 2

<u>Retirement System</u>	<u>Actuarial Valuation Date</u>	<u>Funding Method</u>	<u>Interest Rate (%) Assumptions</u>	<u>Market Value of Assets</u>	<u>Actuarial Liabilities</u>	<u>Actuarial Value of Assets</u>
Knox County Teachers	1/1/2003	AGG	8.00	\$64	\$71	\$71
Los Angeles City ERS	6/30/2003	PUC	8.00	\$5,985	\$7,660	\$7,000
Los Angeles City Fire & Police	6/30/2003	EAN	8.50	\$9,793	\$11,204	\$11,691
City of Los Angeles Water & Power	6/30/2003	EAN	8.00	\$5,559	\$6,042	\$6,128
Los Angeles County ERA	6/30/2003	EAN	8.00	\$26,248	\$30,474	\$26,564
Los Angeles County MTA	12/31/2002	EAN	8.50	\$553	\$747	\$532
Marin County ERA	6/30/2002	EAN	8.25	\$834	\$798	\$712
City of Memphis RS	7/1/2003	FEA	7.50	\$1,692	\$1,994	\$1,862
Milwaukee City ERS	1/1/2003	PUC	8.50	\$3,356	\$3,204	\$3,690
Milwaukee County ERS	1/1/2003	AGG	9.00	\$1,283	\$1,542	\$1,447
Minneapolis ERF	7/1/2003	EAN	6.00	\$1,195	\$1,646	\$1,519
Minneapolis Teachers' RFA	7/1/2003	EAN	8.50	\$720	\$1,672	\$957
Montgomery County ERS	6/30/2002	PUC	8.00	\$1,727	\$2,411	\$2,029
Montgomery County Public Schools	7/1/2003	PUC	8.00	\$602	\$793	\$741
New York City ERS	6/30/2002	FIL	8.00	\$32,842	\$43,620	\$43,561
New York City Police PF	6/30/2002	FIL	8.00	\$14,505	\$18,914	\$18,914
New York City Teachers RS	6/30/2002	FIL	8.00	\$27,026	\$34,181	\$34,178
Norfolk ERS	6/30/2003	PUC	7.50	\$750	\$813	\$761
City of Oakland Police & Fire RS	7/1/2002	AGG	8.00	\$673	\$675	\$675
Oakland County PERS	9/30/2002	AGG	7.50	\$606	\$602	\$723
Oakland County Road Commission PERS	12/31/2002	EAN	7.50	\$131	\$133	\$149
Oklahoma City ERS	12/31/2002	EAN	8.00	\$339	\$373	\$375
Orange County ERS	12/31/2003	PUC	7.50	\$4,960	\$6,099	\$4,790
Orlando Firefighter PF	10/1/2003	EAN	8.00	\$179	\$195	\$189
Orlando GEPP	10/1/2003	AGG	8.00	\$150	\$167	\$158
Orlando Police PF	10/1/2003	EAN	8.00	\$256	\$285	\$249
City of Philadelphia RS	7/1/2002	EAN	9.00	\$3,959	\$6,727	\$4,891
Phoenix ERP	6/30/2003	EAN	8.00	\$1,263	\$1,504	\$1,331
Prince George's County PTF	1/1/2002	EAN	8.00	\$743	\$1,138	\$922
City of Richmond RS	6/30/2003	PUC	8.00	\$400	\$635	\$440
Sacramento City ERS	6/30/2003	EAN	7.50	\$386	\$363	\$386
Sacramento County ERS	6/30/2003	EAN	8.00	\$3,239	\$4,108	\$3,864
San Antonio Police & Fire PF	10/1/2003	EAN	8.00	\$1,327	\$1,718	\$1,429
San Bernadino County ERA	6/30/2003	EAN	8.16	\$3,171	\$4,368	\$3,816
San Diego City ERS	6/30/2002	PUC	8.00	\$2,527	\$3,169	\$2,448
San Diego County ERA	6/30/2003	EAN	8.25	\$4,103	\$5,853	\$4,418
San Francisco City & County RS	6/30/2003	EAN	8.25	\$10,533	\$9,416	\$11,103
San Joaquin County ERA	1/1/2002	EAN	8.25	\$1,366	\$1,267	\$1,357
San Jose Federated City ERS	6/30/2001	EAN	8.25	\$1,105	\$1,072	\$1,060
San Jose Police & Fire Dept RP	6/30/2001	EAN	8.00	\$1,643	\$1,493	\$1,714
San Luis Obispo County PT	1/1/2003	EAN	7.75	\$402	\$556	\$430
San Mateo County ERA	6/30/2003	EAN	8.00	\$1,233	\$1,782	\$1,354
Santa Barbara County ERS	6/30/2003	EAN	8.00	\$1,169	\$1,455	\$1,347
Santa Clara VTA ATU PP	1/1/2003	EAN	8.00	\$222	\$278	\$224
Seattle City ERS	1/1/2004	EAN	7.75	\$1,528	\$1,779	\$1,528
St. Louis County ERP	1/1/2003	PUC	8.00	\$337	\$401	\$312
St. Louis Public School RS	1/1/2003	FEA	8.00	\$854	\$1,063	\$873
St. Paul Teachers' RFA	7/1/2003	EAN	8.50	\$758	\$1,189	\$899
Sonoma County ERA	12/31/2003	EAN	8.00	\$1,110	\$1,130	\$1,100
Tacoma ERS	1/1/2003	EAN	7.75	\$611	\$687	\$740
City of Tallahassee PP	9/30/2001	EAN	7.75	\$749	\$598	\$724
Texas County & District RS	12/31/2003	EAN	8.00	\$10,872	\$10,814	\$9,789
Tulare County ERA	6/30/2003	EAN	8.00	\$640	\$609	\$634
Ventura County ERA	6/30/2003	EAN	8.00	\$1,967	\$2,202	\$2,057
<b>Totals</b>	<b>6/30/2003</b> (median)		<b>8.00</b> (Avg.)	<b>\$200,245</b> (Sum)	<b>\$243,689</b> (Sum)	<b>\$230,855</b> (Sum)

**Appendix IIB**  
**City and County Retirement Systems – Funding Ratio<sup>5</sup>**  
(\$ Millions)

<b>Retirement System</b>	<b>Report Date</b>	<b>Ratio of Assets to Liabilities</b>	<b>Rank Out of 104 Systems</b>	<b>Assets minus Liabilities (\$ millions)</b>	<b>Actuarial Rank Out of 104 Systems</b>
City of Fresno ERS	6/30/2002	1.35	1	\$185	3
City of Fresno Fire & Police RS	6/30/2002	1.34	2	\$198	2
City of Tallahassee PP	9/30/2001	1.25	3	\$151	5
City of Baton Rouge PGT	12/31/2003	1.16	4	\$4	19
San Francisco City & County RS	6/30/2003	1.12	5	\$1,117	1
San Jose Police & Fire Dept RP	6/30/2001	1.10	6	\$151	6
San Joaquin County ERA	12/31/2001	1.08	7	\$99	7
Imperial County ERS	6/30/2003	1.07	8	\$23	15
Sacramento City ERS	6/30/2003	1.06	9	\$23	14
Tulare County ERA	6/30/2003	1.05	10	\$31	11
Milwaukee City ERS	12/31/2002	1.05	11	\$152	4
Marin County ERA	6/30/2002	1.04	12	\$35	9
San Jose Federated City ERS	6/30/2001	1.03	13	\$33	10
Arlington County ERS	6/30/2002	1.03	14	\$29	13
Anne Arundel County ERP	12/31/2003	1.03	15	\$10	17
City of Birmingham R&RS	6/30/2003	1.02	16	\$15	16
Alameda County ERA	12/31/2003	1.01	17	\$30	12
Oakland County PERS	9/30/2002	1.01	18	\$4	18
Texas County & District RS	12/31/2003	1.01	19	\$58	8
Gainesville General EPP	9/30/2003	1.00	20	\$0	20
Anne Arundel County PSRP	12/31/2003	1.00	21	\$0	21
City of Oakland Police & Fire RS	6/30/2002	1.00	22	-\$2	25
Oakland County Road Commission PERS	12/31/2002	0.99	23	-\$1	22
Gainesville Police & Firefighters RP	9/30/2003	0.99	24	-\$1	23
Grand Rapids Police & Fire RS	6/30/2003	0.98	25	-\$4	26
Sonoma County ERA	12/31/2003	0.98	26	-\$19	34
Anne Arundel County FSRP	12/31/2003	0.98	27	-\$7	28
City of Cincinnati RS	12/31/2003	0.95	28	-\$81	44
Denver ERP	12/31/2001	0.95	29	-\$79	43
Norfolk ERS	6/30/2003	0.92	30	-\$63	40
Orlando Firefighter PF	9/30/2003	0.92	31	-\$15	32
City of Los Angeles Water & Power	6/30/2003	0.92	32	-\$483	75
Oklahoma City ERS	6/30/2002	0.91	33	-\$34	37
Grand Rapids GRS	6/30/2003	0.90	34	-\$28	35
Orlando Police PF	9/30/2003	0.90	35	-\$29	36
Orlando GEPP	9/30/2003	0.90	36	-\$17	33
Knox County Teachers	6/30/2003	0.90	37	-\$7	29
Ventura County ERA	6/30/2003	0.89	38	-\$235	57
Jacksonville General EPP	9/30/2003	0.89	39	-\$175	49
Tacoma ERS	12/31/2002	0.89	40	-\$76	42
Baltimore County ERS	6/30/2003	0.89	41	-\$208	54
Anne Arundel County DODSRP	12/31/2003	0.88	42	-\$6	27
Howard County RP	6/30/2002	0.88	43	-\$14	31
Los Angeles City Fire & Police	6/30/2003	0.87	44	-\$1,410	93
Fairfax County Police	6/30/2002	0.87	45	-\$83	45
Baltimore City ERS	6/30/2003	0.87	46	-\$180	51
Los Angeles County ERA	6/30/2003	0.86	47	-\$4,226	101
Denver Public Schools RS	12/31/2003	0.86	48	-\$390	68
Seattle City ERS	12/31/2003	0.86	49	-\$251	59
Knox County	6/30/2003	0.86	50	-\$12	30
Fairfax County Uniformed RS	6/30/2002	0.86	51	-\$103	46
City of Memphis RS	6/30/2003	0.85	52	-\$301	64
Baltimore City Elected Officials RS	6/30/2003	0.84	53	-\$2	24
Houston Firefighters' R&RF	6/30/2002	0.84	54	-\$310	65
Phoenix ERP	6/30/2003	0.84	55	-\$242	58



## Appendix IIB – Page 2 of 2

Retirement System	Report Date	Ratio of Assets to Liabilities	Rank Out of 104 Systems	Assets minus Liabilities (\$ millions)	Actuarial Rank Out of 104 Systems
St. Louis County ERP	12/31/2003	0.84	56	-\$65	41
Fairfax County ERS	6/30/2002	0.84	57	-\$335	66
Milwaukee County ERS	12/31/2002	0.83	58	-\$259	60
City of Baton Rouge & Parish ERS	12/31/2003	0.83	59	-\$172	48
Orange County ERS	12/31/2003	0.81	60	-\$1,140	88
City of Austin ERS	12/31/2003	0.81	61	-\$292	63
Fresno County ERA	6/30/2002	0.81	62	-\$367	67
Chicago Teachers PF	6/30/2003	0.81	63	-\$2,208	97
Santa Barbara County ERS	6/30/2003	0.80	64	-\$285	62
St. Louis Public School RS	12/31/2002	0.80	65	-\$210	55
Santa Clara VTA ATU PP	6/30/2003	0.80	66	-\$56	38
San Diego City ERS	6/30/2002	0.80	67	-\$641	79
New York City Teachers RS	6/30/2002	0.79	68	-\$7,155	103
Sacramento County ERS	6/30/2003	0.79	69	-\$869	85
Los Angeles City ERS	6/30/2003	0.78	70	-\$1,675	94
City of Baltimore Fire & Police	6/30/2003	0.77	71	-\$517	77
Detroit Fire & Police	6/30/2003	0.77	72	-\$843	83
San Antonio Police & Fire PF	9/30/2003	0.77	73	-\$391	69
New York City Police PF	6/30/2002	0.77	74	-\$4,409	102
Montgomery County Public Schools	6/30/2003	0.76	75	-\$191	52
Kern County ERA	6/30/2002	0.76	76	-\$463	74
Dallas Police & Fire	12/31/03	0.76	77	-\$706	82
Fulton County ERS	12/31/2002	0.75	78	-\$267	61
New York City ERS	6/30/2002	0.75	79	-\$10,778	104
Houston Police	6/30/2002	0.75	80	-\$645	80
Los Angeles County MTA	6/30/2002	0.74	81	-\$193	53
Kansas City Police ERS	4/30/2003	0.74	82	-\$180	50
Minneapolis ERF	6/30/2003	0.73	83	-\$451	73
San Bernadino County ERA	6/30/2003	0.73	84	-\$1,198	89
San Luis Obispo County PT	12/31/2002	0.72	85	-\$154	47
Montgomery County ERS	6/30/2003	0.72	86	-\$685	81
Detroit General RS	6/30/2003	0.71	87	-\$947	86
San Diego County ERA	6/30/2003	0.70	88	-\$1,750	95
San Mateo County ERA	6/30/2003	0.69	89	-\$548	78
Fort Worth ERF	9/30/2002	0.68	90	-\$489	76
Chicago Municipal EA&BF	12/31/2002	0.68	91	-\$2,449	98
Prince George's County PTF	6/30/2002	0.65	92	-\$394	70
Howard County Police & Fire ERP	6/30/2002	0.65	93	-\$58	39
Dallas ERF	12/31/2002	0.65	94	-\$845	84
Contra Costa County ERA	12/31/2002	0.64	95	-\$1,312	91
St. Paul Teachers' RFA	6/30/2003	0.64	96	-\$432	71
City of Richmond RS	6/30/2003	0.63	97	-\$235	56
Jacksonville Police & Fire PP	9/30/2003	0.61	98	-\$442	72
City of Boston RS	12/31/2003	0.60	99	-\$2,184	96
City of Philadelphia RS	6/30/2002	0.59	100	-\$2,769	99
Chicago Policemen's ABF	12/31/2002	0.56	101	-\$2,888	100
Houston Municipal EPS	6/30/2002	0.51	102	-\$1,243	90
Chicago Firemen's ABF	12/31/2003	0.44	103	-\$1,408	92
Minneapolis Teachers' RFA	6/30/2003	0.43	104	-\$952	87
<b>Totals</b>	<b>6/30/2003</b> (Median)	<b>0.85</b> (Avg.)			

### Appendix IIIA

#### State Retirement Systems – Actuarial Summary<sup>6</sup>

(\$ Millions)

Retirement System	Actuarial Valuation Date	Funding Method	Interest Rate (%) Assumptions	Market Value of Assets	Actuarial Liabilities	Actuarial Value of Assets
Alabama ERS	9/30/2001	EAN	8.00	\$7,460	\$8,299	\$8,274
Alabama Teachers	6/30/2002	EAN	8.00	\$14,168	\$18,374	\$17,905
Alaska PERS	6/30/2002	EAN	8.00	\$5,324	\$6,133	\$4,611
Alaska Teachers	6/30/2002	PUC	8.25	\$2,983	\$3,960	\$2,699
Arizona SRS	6/30/2002	PUC	8.00	\$18,347	\$21,285	\$22,642
Arkansas Highway ERS	6/30/2003	EAN	8.00	\$891	\$976	\$1,040
Arkansas PERS	6/30/2003	EAN	8.00	\$3,883	\$4,674	\$4,416
Arkansas Teachers	6/30/2002	EAN	8.00	\$7,084	\$9,062	\$8,328
California PERS	6/30/2002	EAN	8.25	\$142,787	\$163,961	\$156,067
California Regents	6/30/2003	EAN	7.50	\$35,327	\$32,955	\$41,429
California Teachers	6/30/2001	EAN	8.00	\$103,138	\$109,881	\$107,654
Colorado Fire & Police	12/31/2002	EAN	8.00	\$2,083	\$2,667	\$2,571
Colorado State & School	12/31/2002	EAN	8.75	\$22,149	\$32,630	\$28,715
Colorado Municipal Division	12/31/2002	EAN	8.75	\$1,423	\$1,966	\$1,840
Connecticut PERS	6/30/2002	PUC	8.50	\$7,091	\$12,806	\$7,894
Connecticut Teachers	6/30/2002	EAN	8.50	\$10,126	\$13,680	\$10,387
Delaware PERS	6/30/2003	EAN	8.50	\$4,845	\$5,314	\$4,845
DC PERS	10/1/2000	AGG	7.25	\$1,179	\$2,093	\$1,097
DC Teachers	10/1/2002	AGG	7.25	\$826	\$1,055	\$799
Florida RS	7/1/2002	EAN	8.00	\$89,529	\$86,470	\$99,406
Georgia PERS	6/30/2001	EAN	7.00	\$13,345	\$12,348	\$12,704
Georgia Teachers	6/30/2002	EAN	7.25	\$37,831	\$39,707	\$40,502
Hawaii ERS	6/30/2003	EAN	8.00	\$7,687	\$11,952	\$9,074
Idaho PERS	7/1/2003	EAN	8.00	\$6,499	\$7,890	\$6,481
Illinois PERS	6/30/2003	PUC	8.50	\$7,882	\$18,867	\$7,882
Illinois SURS	6/30/2003	PUC	8.50	\$9,715	\$18,025	\$9,715
Illinois Teachers	6/30/2003	PUC	8.50	\$23,125	\$46,933	\$23,125
Indiana PERS	7/1/2001	EAN	7.25	\$8,519	\$8,572	\$8,891
Indiana Police & Fire	7/1/2001	EAN	7.50	\$1,533	\$1,620	\$1,491
Indiana Teachers	6/30/2003	EAN	7.50	\$6,156	\$14,747	\$6,554
Iowa Fire & Police	7/1/2003	AGG	7.50	\$1,137	\$1,370	\$1,255
Iowa PERS	6/30/2003	EAN	7.50	\$15,403	\$17,987	\$16,120
Kansas PERS	12/31/2002	PUC	8.00	\$8,930	\$12,614	\$9,785
Kentucky PERS	6/30/2003	EAN	8.25	\$5,569	\$7,292	\$7,150
Kentucky Counties	6/30/2003	EAN	8.25	\$5,345	\$5,917	\$6,754
Kentucky Teachers	6/30/2003	PUC	7.50	\$12,043	\$16,595	\$13,864
Louisiana Municipal Police	6/30/2003	EAN	7.00	\$1,106	\$1,456	\$1,076
Louisiana PERS	6/30/2003	PUC	8.25	\$5,719	\$9,796	\$6,488
Louisiana Teachers	6/30/2003	PUC	8.25	\$10,521	\$17,173	\$11,827
Maine PERS	6/30/2001	EAN	8.00	\$2,169	\$2,857	\$2,292
Maine Teachers	6/30/2001	EAN	8.00	\$3,322	\$5,102	\$3,510
Maryland PERS	6/30/2003	EAN	7.75	\$9,623	\$12,760	\$11,709
Maryland State Police	6/30/2003	EAN	7.75	\$996	\$1,062	\$1,285
Maryland Teachers	6/30/2003	EAN	7.75	\$16,108	\$21,152	\$19,627
Massachusetts PERS	1/1/2003	EAN	8.25	\$12,128	\$17,551	\$13,947
Massachusetts Teachers	1/1/2003	EAN	8.25	\$12,837	\$22,892	\$14,762
Michigan Municipal	12/31/2001	EAN	8.00	\$3,648	\$4,784	\$4,034
Michigan SERS	9/30/2002	EAN	8.00	\$8,509	\$10,988	\$10,908
Michigan Police	9/30/2002	EAN	8.00	\$888	\$1,136	\$1,141
Michigan Teachers	9/30/2002	EAN	8.00	\$30,008	\$41,957	\$38,382
Minnesota PERA	6/30/2003	EAN	8.50	\$8,887	\$13,839	\$11,252
Minnesota Police & Fire	6/30/2003	EAN	8.50	\$3,708	\$4,391	\$4,714
Minnesota SRS	6/30/2003	EAN	8.50	\$6,685	\$8,492	\$8,362
Minnesota State Patrol	6/30/2002	EAN	8.50	\$476	\$510	\$591
Minnesota Teachers	7/1/2003	EAN	8.50	\$13,602	\$16,856	\$17,384

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Mississippi PERS	6/30/2003	EAN	8.00	\$14,444	\$21,800	\$17,249
Missouri Highway ERS	6/30/2001	EAN	8.25	\$1,413	\$2,301	\$1,521
Missouri PERS	6/30/2003	EAN	8.50	\$5,235	\$6,949	\$6,108
Missouri Teachers	6/30/2003	EAN	8.00	\$20,048	\$24,719	\$20,048
Missouri Non-Teachers School	6/30/2003	EAN	8.00	\$1,678	\$2,050	\$1,678
Montana PERS	6/30/2002	EAN	8.00	\$3,069	\$3,816	\$3,680
Montana Teachers	7/1/2002	EAN	8.00	\$2,042	\$2,980	\$2,485
Nebraska RS	7/1/2003	EAN	8.00	\$4,544	\$5,761	\$5,259
Nevada PERS	6/30/2003	EAN	8.00	\$14,074	\$19,541	\$15,883
New Hampshire PERS	6/30/2003	AGG	9.00	\$1,224	\$1,991	\$1,391
New Hampshire Police	6/30/2003	AGG	9.00	\$590	\$852	\$656
New Hampshire Teachers	6/30/2003	AGG	9.00	\$1,310	\$1,827	\$1,453
New Jersey PERS	6/30/2001	PUC	8.75	\$24,788	\$24,133	\$28,186
New Jersey Police & Fire	6/30/2001	PUC	8.75	\$16,789	\$17,923	\$18,074
New Jersey State Police	6/30/2001	PUC	8.75	\$1,762	\$1,627	\$1,829
New Jersey Teachers	6/30/2001	PUC	8.75	\$30,930	\$32,745	\$35,351
New Mexico PERA	6/30/2003	EAN	8.00	\$8,198	\$9,356	\$9,103
New Mexico Teachers	6/30/2003	EAN	8.00	\$6,083	\$9,267	\$7,518
New York PERS	4/1/2003	AGG	8.00	\$82,555	\$107,610	\$107,610
New York Police & Fire	4/1/2003	AGG	8.00	\$14,817	\$19,412	\$19,412
New York STRS	6/30/2002	AGG	8.00	\$73,041	\$71,693	\$71,374
North Carolina PERS	12/31/2003	EAN	7.25	\$45,254	\$38,230	\$42,641
North Carolina Local	12/31/2001	FEA	7.25	\$11,487	\$10,836	\$10,764
North Dakota PERS	6/30/2003	EAN	8.00	\$1,130	\$1,231	\$1,206
North Dakota Teachers	7/1/2003	EAN	8.00	\$1,175	\$1,690	\$1,438
Ohio PERS	12/31/2001	EAN	8.00	\$44,036	\$47,492	\$48,748
Ohio Police & Fire	1/1/2002	EAN	8.25	\$8,263	\$9,786	\$9,076
Ohio SERS	6/30/2003	EAN	8.25	\$7,096	\$10,634	\$8,772
Ohio STRS	7/1/2003	EAN	8.00	\$44,803	\$65,936	\$48,899
Oklahoma Firefighters	6/30/2003	EAN	7.50	\$1,247	\$1,947	\$1,497
Oklahoma PERS	7/1/2003	EAN	7.50	\$4,619	\$6,975	\$5,355
Oklahoma Police	6/30/2003	EAN	7.50	\$1,153	\$1,647	\$1,392
Oklahoma Teachers	6/30/2003	EAN	8.00	\$5,863	\$11,925	\$6,437
Oregon PERS	12/31/2002	EAN	8.00	\$37,041	\$39,521	\$35,537
Pennsylvania ERS	12/31/2002	EAN	8.50	\$20,880	\$25,650	\$27,498
Pennsylvania Teachers	6/30/2002	EAN	8.50	\$43,473	\$51,797	\$54,296
Rhode Island ERS	6/30/2002	EAN	8.25	\$1,955	\$3,323	\$2,383
Rhode Island Municipal	6/30/2002	EAN	8.25	\$706	\$815	\$907
Rhode Island Teachers	6/30/2002	EAN	8.25	\$2,754	\$4,855	\$3,554
South Carolina RS	7/1/2002	EAN	7.25	\$18,678	\$22,686	\$19,442
South Carolina Police	7/1/2002	EAN	7.25	\$2,274	\$2,528	\$2,351
South Dakota RS	6/30/2003	EAN	8.00	\$4,784	\$4,819	\$4,686
Tennessee SETHEPP	7/1/2001	FEA	7.50	\$20,578	\$20,842	\$20,761
Tennessee PSPP	7/1/2001	FEA	7.50	\$3,160	\$3,528	\$3,188
Texas CDRS	12/31/2002	EAN	8.00	\$8,902	\$9,898	\$8,779
Texas ERS	8/31/2003	EAN	8.00	\$17,582	\$20,333	\$19,608
Texas LECOSRF	8/31/2003	EAN	8.00	\$594	\$598	\$667
Texas Municipal	12/31/2001	PUC	8.00	\$8,635	\$10,867	\$9,237
Texas Teachers	8/31/2003	EAN	8.00	\$77,633	\$94,263	\$89,033
Utah Noncontributory	12/31/2002	EAN	7.00	\$9,158	\$11,730	\$10,990

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<b>Retirement System</b>	<b>Actuarial Valuation Date</b>	<b>Funding Method</b>	<b>Interest Rate (%) Assumptions</b>	<b>Market Value of Assets</b>	<b>Actuarial Liabilities</b>	<b>Actuarial Value of Assets</b>
Utah Contributory	12/31/2002	EAN	7.00	\$716	\$975	\$859
Utah Public Safety	12/31/2002	EAN	7.00	\$1,125	\$1,474	\$1,349
Utah Firefighters	12/31/2002	EAN	7.00	\$461	\$530	\$554
Vermont SRS	6/30/2003	EAN	8.00	\$1,115	\$1,271	\$1,248
Vermont Teachers	6/30/2003	EAN	8.00	\$1,099	\$1,359	\$1,218
Virginia RS	6/30/2002	EAN	8.00	\$33,456	\$40,018	\$40,165
Washington PERS 1	9/30/2002	EAN	8.00	\$8,649	\$12,560	\$10,757
Washington PERS 2	9/30/2002	AGG	8.00	\$9,210	\$10,799	\$10,714
Washington LEOFF 1	9/30/2002	EAN	8.00	\$4,317	\$4,259	\$5,095
Washington LEOFF 2	9/30/2002	AGG	8.00	\$2,445	\$2,646	\$2,646
Washington WSPRS	9/30/2002	AGG	8.00	\$596	\$689	\$689
Washington SERS 2 & 3	9/30/2002	AGG	8.00	\$1,301	\$1,519	\$1,519
Washington TRS 1	9/30/2002	EAN	8.00	\$7,335	\$10,235	\$9,366
Washington TRS 2 & 3	9/30/2002	AGG	8.00	\$3,220	\$3,800	\$3,800
West Virginia PERS	7/1/2002	EAN	7.50	\$2,589	\$3,432	\$2,589
West Virginia Teachers	7/1/2002	EAN	7.50	\$1,098	\$5,709	\$1,098
Wisconsin RS	12/31/2002	FEA	8.00	\$51,741	\$59,619	\$57,862
Wyoming RS	1/1/2003	EAN	8.00	\$4,084	\$5,299	\$4,897
<b>Totals</b>	<b>9/30/2002</b> (Median)		<b>7.78</b> (Avg.)	<b>\$134,557</b> (Sum)	<b>\$166,193</b> (Sum)	<b>\$156,425</b> (Sum)

EAN = Entry Age Normal  
 AGG = Aggregate Cost  
 FEA = Frozen Entry Age  
 PUC = Projected Unit Credit

## Appendix IIIB

### State Retirement Systems – Funding Ratio<sup>6</sup>

(\$ Millions)

<u>Retirement System</u>	<u>Ratio of Assets to (at market value) Liabilities</u>	<u>Rank Out of 123 Pension Systems</u>	<u>Assets minus Liabilities (in \$ millions)</u>	<u>Rank Out of 123 Pension Systems</u>
North Carolina PERS	1.18	1	\$7,024	1
New Jersey State Police	1.08	2	\$135	8
Georgia PERS	1.08	3	\$997	5
California Regents	1.07	4	\$2,372	3
North Carolina Local	1.06	5	\$651	7
Florida RS	1.04	6	\$3,059	2
New Jersey PERS	1.03	7	\$655	6
New York STRS	1.02	8	\$1,348	4
Washington LEOFF 1	1.01	9	\$58	9
Indiana PERS	0.99	10	-\$53	13
Texas LECOSRF	0.99	11	-\$4	10
South Dakota RS	0.99	12	-\$35	12
Tennessee SETHEPP	0.99	13	-\$264	31
Georgia Teachers	0.95	14	-\$1,875	72
Indiana Police & Fire	0.95	15	-\$87	17
New Jersey Teachers	0.94	16	-\$1,815	71
California Teachers	0.94	17	-\$6,743	109
Maryland State Police	0.94	18	-\$66	14
Oregon PERS	0.94	19	-\$2,479	78
New Jersey Police & Fire	0.94	20	-\$1,133	58
Minnesota State Patrol	0.93	21	-\$34	11
Ohio PERS	0.93	22	-\$3,456	87
Washington LEOFF 2	0.92	23	-\$201	22
North Dakota PERS	0.92	24	-\$101	19
Arkansas Highway ERS	0.91	25	-\$85	16
Delaware PERS	0.91	26	-\$469	36
Kentucky Counties	0.90	27	-\$573	41
South Carolina Police	0.90	28	-\$254	27
Texas CDRS	0.90	29	-\$997	57
Alabama ERS	0.90	30	-\$839	51
Tennessee PSPP	0.90	31	-\$368	34
Vermont SRS	0.88	32	-\$155	21
New Mexico PERA	0.88	33	-\$1,157	60
California PERS	0.87	34	-\$21,174	121
Utah Firefighters	0.87	35	-\$69	15
Alaska PERS	0.87	36	-\$809	50
Wisconsin RS	0.87	37	-\$7,878	111
Rhode Island Municipal	0.87	38	-\$109	20
Washington WSPRS	0.86	39	-\$93	18
Texas ERS	0.86	40	-\$2,751	81
Arizona SRS	0.86	41	-\$2,938	83
Washington SERS 2 & 3	0.86	42	-\$218	23
Iowa PERS	0.86	43	-\$2,584	80
Washington PERS 2	0.85	44	-\$1,588	66
Washington TRS 2 & 3	0.85	45	-\$581	42
Minnesota Police & Fire	0.84	46	-\$683	44
Ohio Police & Fire	0.84	47	-\$1,523	65
Pennsylvania Teachers	0.84	48	-\$8,323	113
Virginia RS	0.84	49	-\$6,562	107
Arkansas PERS	0.83	50	-\$791	49

## Appendix IIIB – Page 2 of 3

<b>Retirement System</b>	<b>Ratio of Assets to (at market value) Liabilities</b>	<b>Rank Out of 123 Pension Systems</b>	<b>Assets minus Liabilities (in \$ millions)</b>	<b>Rank Out of 123 Pension Systems</b>
Iowa Fire & Police	0.83	51	-\$233	25
Idaho PERS	0.82	52	-\$1,391	64
Texas Teachers	0.82	53	-\$16,630	119
South Carolina RS	0.82	54	-\$4,008	92
Missouri Non-Teachers School	0.82	55	-\$372	35
Pennsylvania ERS	0.81	56	-\$4,771	100
Missouri Teachers	0.81	57	-\$4,671	99
Vermont Teachers	0.81	58	-\$260	29
Minnesota Teachers	0.81	59	-\$3,255	86
Montana PERS	0.80	60	-\$747	47
Texas Municipal	0.79	61	-\$2,232	15
Nebraska RS	0.79	62	-\$1,217	62
Minnesota SRS	0.79	63	-\$1,806	70
DC Teachers	0.78	64	-\$228	24
Michigan Police	0.78	65	-\$247	26
Arkansas Teachers	0.78	66	-\$1,977	73
Colorado Fire & Police	0.78	67	-\$584	43
Utah Noncontributory	0.78	68	-\$2,571	79
Michigan SERS	0.77	69	-\$2,479	77
Alabama Teachers	0.77	70	\$4,206	94
Wyoming RS	0.77	71	-\$1,215	61
New York PERS	0.77	72	-\$25,055	123
Kentucky PERS	0.76	73	-\$1,723	68
New York Police & Fire	0.76	74	-\$4,595	97
Utah Public Safety	0.76	75	-\$349	32
Michigan Municipal	0.76	76	-\$1,136	59
Maryland Teachers	0.76	77	-\$5,044	102
Louisiana Municipal Police	0.76	78	-\$349	33
Maine PERS	0.76	79	-\$688	45
West Virginia PERS	0.75	80	-\$844	52
Maryland PERS	0.75	81	-\$3,137	84
Alaska Teachers	0.75	82	-\$977	56
Missouri PERS	0.75	83	-\$1,714	67
Connecticut Teachers	0.74	84	-\$3,554	89
Utah Contributory	0.73	85	-\$259	28
Kentucky Teachers	0.73	86	-\$4,552	96
Colorado Municipal Division	0.72	87	-\$543	40
Nevada PERS	0.72	88	-\$5,467	104
New Hampshire Teachers	0.72	89	-\$516	39
Washington TRS 1	0.72	90	-\$2,900	82
Michigan Teachers	0.72	91	-\$11,949	118
Kansas PERS	0.71	92	-\$3,683	90
Oklahoma Police	0.70	93	-\$494	37
North Dakota Teachers	0.70	94	-\$515	38
New Hampshire Police	0.69	95	-\$261	30
Massachusetts PERS	0.69	96	-\$5,423	103
Washington PERS 1	0.69	97	-\$3,911	91
Montana Teachers	0.69	98	-\$938	55
Ohio STRS	0.68	99	-\$21,134	120
Colorado State & School	0.68	100	-\$10,480	116

### Appendix IIIB – Page 3 of 3

<u>Retirement System</u>	<u>Ratio of Assets to (at market value) Liabilities</u>	<u>Rank Out of 123 Pension Systems</u>	<u>Assets minus Liabilities (in \$ millions)</u>	<u>Rank Out of 123 Pension Systems</u>
Ohio SERS	0.67	101	-\$3,538	88
Mississippi PERS	0.66	102	-\$7,356	110
Oklahoma PERS	0.66	103	-\$2,356	76
New Mexico Teachers	0.66	104	-\$3,183	85
Maine Teachers	0.65	105	-\$1,780	69
Hawaii ERS	0.64	106	-\$4,265	95
Minnesota PERA	0.64	107	-\$4,952	101
Oklahoma Firefighters	0.64	108	-\$699	46
New Hampshire PERS	0.61	109	-\$767	48
Missouri Highway ERS	0.61	110	-\$888	53
Louisiana Teachers	0.61	111	-\$6,653	108
Rhode Island ERS	0.59	112	-\$1,368	63
Louisiana PERS	0.58	113	-\$4,078	93
Rhode Island Teachers	0.57	114	-\$2,101	74
DC PERS	0.56	115	-\$914	54
Massachusetts Teachers	0.56	116	-\$10,055	115
Connecticut PERS	0.55	117	-\$5,716	105
Illinois SURS	0.54	118	-\$8,310	112
Illinois Teachers	0.49	119	-\$23,809	122
Oklahoma Teachers	0.49	120	-\$6,062	106
Illinois PERS	0.42	121	-\$10,985	117
Indiana Teachers	0.42	122	\$8,592	114
West Virginia Teachers	0.19	123	-\$4,611	98
<b>Total</b>	<b>0.79</b> (Avg.)			

## Appendix IV

### MUNICIPAL BANKRUPTCY

Municipal bankruptcy has been controversial since its inception in the 1930's, largely due to constitutional conflicts between state and federal powers. Thus, the laws governing municipal bankruptcy are more ambiguous than the laws for private sector bankruptcy. In addition to conflicting state and federal laws, there are differing opinions regarding which of a number of State of Michigan laws (which also can be conflicting) related to municipal bankruptcy would apply.

#### STEPS REQUIRED TO DECLARE BANKRUPTCY

A municipality may declare bankruptcy under Chapter 9 of the Federal Bankruptcy Code, entitled “Adjustment of Debts of a Municipality” (as distinguished from discharge of debts in a private sector Chapter 7 bankruptcy). The applicable State must consent to the bankruptcy proceedings before they can commence.

In Michigan, the following administrative remedies need to be exhausted before such consent is given:

- “The Local Government Fiscal Responsibility Act” (Public Act 72 of 1990) grants the State authority to “take over” struggling municipalities whenever a “local government financial emergency” exists as declared by the Governor, after a detailed audit and review process. The law then provides for establishing an “Emergency Financial Manager” (EFM) for such a municipality.
- The “Emergency Municipal Loan Act” (Public Act 243 of 1980) allows loans by the State of not more than \$5,000,000 to any one municipality to aid in the “local financial emergency”. This \$5,000,000 maximum makes this Act irrelevant for the City of Detroit.

If the EFM finds that the municipality is a “lost cause”, the EFM would give written notice to the “Local Emergency Financial Assistance Loan Board”. Assuming that the Board does not disapprove the notice within 60 days of its receipt, the EFM would authorize the municipality to file bankruptcy under Chapter 9.

#### IMPACT OF CHAPTER 9 BANKRUPTCY ON PENSION AND OTHER BENEFITS

Chapter 9 MAY give a municipality the right to re-negotiate its collective bargaining agreements, including all matters therein related to retiree pensions, health care, and other post-retirement benefits.



### Federal Law

Section 926 of the Federal Bankruptcy Act, known as the “Avoiding Powers” provision gives a debtor the ability to avoid certain existing executory contracts (including collective bargaining agreements between the municipality and its employees) during the Chapter 9 proceedings. (Section 926 further provides that if the debtor should refuse to exercise such rights then a creditor may request that the court order the bankruptcy trustee to pursue such rights.)

Specifically, legislative statements (Senate Report No. 95-989) state that such contracts may be rejected despite contrary State laws. Courts should readily allow the rejection of such contracts where: they are burdensome, the rejection will aid in the municipality’s reorganization, and in consideration of the equities of each case. Equities in favor of a municipality in Chapter 9 will be far more compelling than the equities in favor of a private employer in Chapter 11.

Onerous employment obligations may prevent a municipality from balancing its budget for some time. Because municipalities have often seemed immune to the constraint of profitability faced by private employers, municipal wage contracts may be relatively more onerous than those in the private sector. It is intended that the power granted in Section 926 to reject collective bargaining agreements will pre-empt State termination provisions, but not State collective bargaining laws.

### Areas of Ambiguity

Despite the seeming clarity of the federal legislation and related legislative statements on conditions in effect after a municipality has filed Chapter 9, the ability to change retiree health care and other benefits remains unclear.

After a Chapter 9 filing, Michigan State laws could still affect the ability of the City to change retiree health care and other benefits. Specifically, pension benefits can vest by operation of common law as it relates to the collective bargaining agreements, actual pension documents, ordinances, etc. The City could well face a strong argument (at least regarding pension benefits) that such benefits are not part of any executory contracts (including collective bargaining agreements) and thus cannot be affected by Chapter 9 proceedings.

In addition, the Michigan State Constitution (Article IX, Section 24) states that:

- The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby.
- Financial benefits arising on account of service rendered in each fiscal year shall be funded during that year, and such funding shall not be used for financing unfunded accrued liabilities.